

JULY 5TH–11TH 2008

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John McCain's lurch to the right

Stockmarkets in the bears' claws

Colombia's hostage success

Britain's sinking economy

The science of pesticides

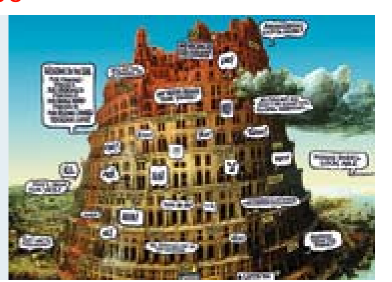
What a way to run the world

Home
This week's print edition
Daily news analysis
Opinion
All opinion
Leaders
Letters to the Editor
Blogs
Columns
KAL's cartoons
Correspondent's diary
Economist debates
World politics
All world politics
Politics this week
International
United States
The Americas
Asia
Middle East and Africa
Europe
Britain
Special reports
Business
All business
Business this week
Management
Business education
Finance and economics
All finance and economics
Economics focus
Economics A-Z
Markets and data
All markets and data
Daily chart
Weekly indicators
World markets
Currencies
Rankings
Big Mac index
Science and technology
All science and technology
Technology Quarterly
Books and arts
All books and arts
Style guide
People
People
Obituaries
Diversions
Audio and video
Audio and video library
Audio edition
Research tools
All research tools
Articles by subject
Backgrounders
Economics A-Z
Special reports
Style guide
Country briefings
All country briefings
China
India
Brazil
United States
Russia
Cities guide

Print Edition July 5th 2008

What a way to run the world

Global institutions are an outdated muddle; the rise of Asia makes their reform a priority for the West: leader



Previous print editions

Jun 28th 2008
Jun 21st 2008
Jun 14th 2008
Jun 7th 2008
May 31st 2008

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Middle East & Africa

Zimbabwe
Africa's shame

Somalia
Continuing to fail

Africa and Coca-Cola
Index of happiness?

Israel's prisoner swaps
A dubious trade

Iran's confrontation with the West
Dangerous games

Clarification: Morgan Tsvangirai

Europe

Spain
¿Crisis? ¿What crisis?

France's Socialists
Left and ultra-left

Corruption in Romania
In denial

Nordic defence
Pooling resources

Georgia, Abkhazia and Russia
Tales from the Black Sea

Charlemagne
The French connection

Britain

Housing slump
Collateral damage

Homebuilders
Throwing in the keys

Health-care reform
Keyhole operation

Royalties on art
Sharing the wealth

Scottish politics
A hard pounding for Mr Brown?

Student politics
Old heads on young shoulders

David Davis
The free vote

Bagehot
The shock of the old

Articles flagged with this icon are printed only in the British edition of *The Economist*

International

Conflict resolution
The discreet charms of the international go-between

Mediation and faith
Not a sword, but peace

The lightness of being

Obituary

Sam Manekshaw

Economic and Financial Indicators

Overview

Output, prices and jobs

The Economist commodity-price index

The Economist poll of forecasters, July averages

Trade, exchange rates, budget balances and interest rates

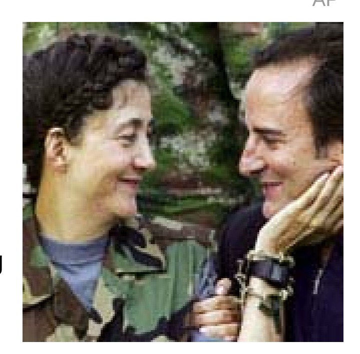
Markets

Foreign direct investment

Politics this week

Jul 3rd 2008
From The Economist print edition

AP



Colombian troops freed **Ingrid Betancourt** and 14 other hostages (including three American military contractors) who were being held by left-wing FARC guerrillas. Ms Betancourt, a Colombian politician who also has French nationality, was kidnapped in 2002 while campaigning for the presidency. She was rescued by army intelligence agents who tricked her captors into believing they were acting on behalf of the FARC's leader. The operation was a political triumph for Colombia's president, Álvaro Uribe. See article

President Uribe's government earlier said it would send a bill to Congress calling for a referendum on re-running **Colombia's** 2006 presidential election. The Supreme Court had questioned the legality of a constitutional amendment that allowed Mr Uribe as a sitting president to seek a second consecutive term.

In another diplomatic spat in the **Andes**, Peru recalled its ambassador to Bolivia after Bolivia's socialist president, Evo Morales, accused Peru of allowing a secret United States military base on its territory. Both Peru and the United States strongly denied the claim.

Some 55% of **Cuba's** farmland is idle or underutilised, up from 46% in 2002, according to a study by the government statistics office. Since he became Cuba's president in February, Raúl Castro has begun turning state land over to private farmers in an effort to cut a $2 billion annual bill for food imports.

Mugabe muscles a win

Robert Mugabe won **Zimbabwe's** presidential run-off election on June 27th. He was unopposed after the other contender, Morgan Tsvangirai, pulled out because of violence and intimidation. The result was widely condemned, but African Union leaders meeting in Egypt did not question the legitimacy of the election and asked for mediation talks between Mr Mugabe and the opposition to continue, with the goal of forming a national-unity government. See article

A **Palestinian** man drove a bulldozer into a bus and several cars in Jerusalem, killing three people and wounding dozens before being shot dead.

Hizbullah, Lebanon's Shia militia, and **Israel** agreed a prisoner swap; Hizbullah will hand over the two Israeli soldiers (who were assumed to be dead) whose capture triggered Israel's offensive in Lebanon in 2006, in return for five Lebanese prisoners. The deal could pave the way for Israel to do the same with Hamas, the Islamist movement that controls Gaza. See article

The usual suspect

Anwar Ibrahim, leader of the opposition in **Malaysia**, briefly took refuge in the Turkish embassy in Kuala Lumpur. He said he feared for his safety after a young male volunteer to his political campaign accused him of sexual assault. Mr Anwar denied the charge, which recalled allegations made in 1998 and later thrown out. On leaving the embassy, he spoke to a large rally. See article

A state of emergency was declared as at least five people died in clashes in **Mongolia's** capital, Ulan Bator. The violence came as the opposition protested against alleged ballot-rigging by the ruling Mongolian People's Revolutionary Party in an election. See article

Talks between representatives of the Dalai Lama, **Tibet's** exiled spiritual leader, and the Chinese government resumed in Beijing. It was the second round of talks since Tibet was wracked by anti-Chinese rioting in March.

Protests continued in the **South Korean** capital, Seoul, against the resumption of imports of beef from America. Police used water-cannon and tear-gas to disperse a crowd as Condoleezza Rice, America's secretary of state, visited. Later, workers staged a two-hour strike in protest at the imports.

India published a "national action plan" on climate change. It promised a new emphasis on renewable energy, but did not include specific targets for cutting carbon emissions.

The government of the Indian state of **Jammu & Kashmir** reversed its decision to transfer land to a board that manages a Hindu shrine. The transfer had provoked some of the biggest separatist protests seen in Kashmir for years. Its revocation prompted counter-protests by Hindu nationalists. See article

Enemies of the (French) state

France took over the European Union's rotating presidency. President Nicolas Sarkozy marked the occasion with fresh attacks on Peter Mandelson, the (British) trade commissioner, who is seeking to cut farm subsidies in world trade talks, and on the European Central Bank, which is raising interest rates. See article

The **French** defence chief resigned two days after a soldier at a military show had mistakenly used live bullets, injuring 16 spectators.

Poland's president, Lech Kaczynski, cast a cloud over France's EU presidency by saying that it would be "pointless" to sign the Lisbon treaty since Irish voters have rejected it. The Polish parliament has at least ratified Lisbon, unlike the Czechs, who are awaiting a court ruling.

Turkey arrested 21 hardline nationalists, including two retired generals, in an investigation into an anti-government plot. The arrests came just before the constitutional court began hearing a case brought by the chief prosecutor, who wants to ban the ruling Justice and Development Party for supposedly trying to bring in Islamic rule.

Plus ça change...

Barack Obama took more strides towards the centre ground of American politics. In a speech in Missouri he spoke about his patriotism and said he would "not stand idly by" when others questioned it. Later, he promised to expand the use of faith-based programmes, which are championed by religious folk. See article

John McCain shook up his team, promoting Steve Schmidt, who has worked for George Bush and Arnold Schwarzenegger, to take full operational control. Republicans are concerned that Mr McCain is not co-ordinating his campaign strategy and pronouncements very well.

After the Supreme Court ruled that a long-standing ban on **handguns** in Washington, DC, was unconstitutional, the National Rifle Association lodged lawsuits against other big cities to get them to overturn their restrictions on guns. See article

AP



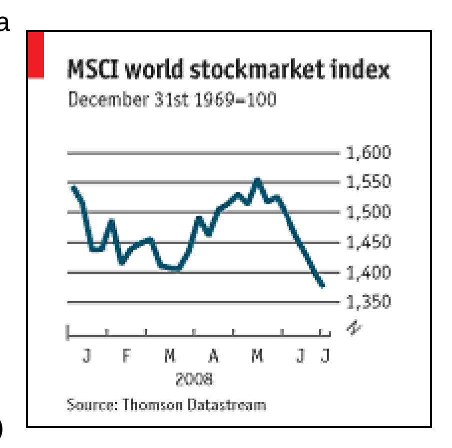
Wildfires along California's scenic coast forced the evacuation of the popular tourist area around **Big Sur**.

Business this week

Jul 3rd 2008
From The Economist print edition

UBS made some changes to its corporate-governance procedures and announced that four directors would leave its board in October. The Swiss bank has been hit hard by the problems in subprime markets, writing down some $38 billion so far; its management has been criticised by shareholders and regulators for failing to spot the crisis. The bank's troubles are not over yet. Investors expect further write-downs and American authorities are investigating allegations that UBS helped wealthy clients to evade taxes. See article

Stockmarkets around the world endured another joyless week, capping a gloomy first half of the year for investors. Since the start of the year, the Dow Jones Industrial Average has fallen by 14%, and the main indices in Britain, France and Germany have dropped by 13%, 21% and 20% respectively. But it is 2007's star performers that have suffered the most. India's main stockmarket was down by 34% since the new year, and China's by 48%. See article



In the grip of a credit squeeze

Bad news from two of Britain's leading companies frightened investors in the City. **Taylor Wimpey** said it had failed to raise the £500m ($1 billion) it sought to bolster its capital position; the homebuilder also warned of a "significant downturn" in its markets. And **Marks & Spencer** issued a surprise profit warning when it reported a drop in sales at its stores and said that it expected consumers to remain cautious with their spending for some time yet. The share prices of both companies plunged. See article

China tightened its capital controls in an effort to curb speculative inflows betting on a rising yuan. Exporters will have to put their export revenues in temporary accounts and prove they come from genuine trade transactions rather than disguised "hot money" inflows. (By exaggerating their export invoices, firms have been bringing in foreign currency to invest in the yuan.) The flood of foreign currency has made it hard for China to control monetary growth and hence inflation.

Richard Grasso won his appeal against a court ruling that would have forced him to return some of the $187.5m pay package he was given when he left his job as the boss of the New York Stock Exchange in 2003. The state of New York said it would no longer pursue the case. Separately, **UnitedHealth Group** agreed to pay $912m to settle shareholders' lawsuits that stem from an options-backdating case.

Samuel Israel, the co-founder of Bayou Management, a bankrupt hedge fund, surrendered in Massachusetts to authorities after three weeks on the run. In April Mr Israel was sentenced to 20 years in prison for defrauding investors. He fled in early June, shortly before he was due to start his sentence.

Too much of a good thing

Starbucks said it would close another 500 coffee shops in the United States, in addition to the 100 it flagged earlier this year. Up to 12,000 full- and part-time jobs will go at the ubiquitous chain, which is suffering from having over expanded in urban areas. See article

Yahoo! gave its side of the story about **Microsoft's** recently failed takeover offer, in a presentation sent to shareholders in preparation for the annual meeting on August 1st. Yahoo! forcefully defended its board and criticised **Carl Icahn**, an activist investor who has nominated his own slate of directors and wants to oust Jerry Yang, Yahoo!'s chief executive.

A French court ordered **eBay** to pay **LVMH** almost €40m ($61m) for failing to stop the sale of fake copies of the luxury-goods giant's products on its website. The court also issued an injunction to stop sales on

eBay of (genuine) perfume brands owned by LVMH. The court's ruling is the biggest challenge yet to eBay's contention that it does not have a legal responsibility for items sold on its site; it will appeal against the court's decision.

France Telecom ditched its $40 billion offer for **TeliaSonera**, less than a month after launching the bid.

Workers of the world unite

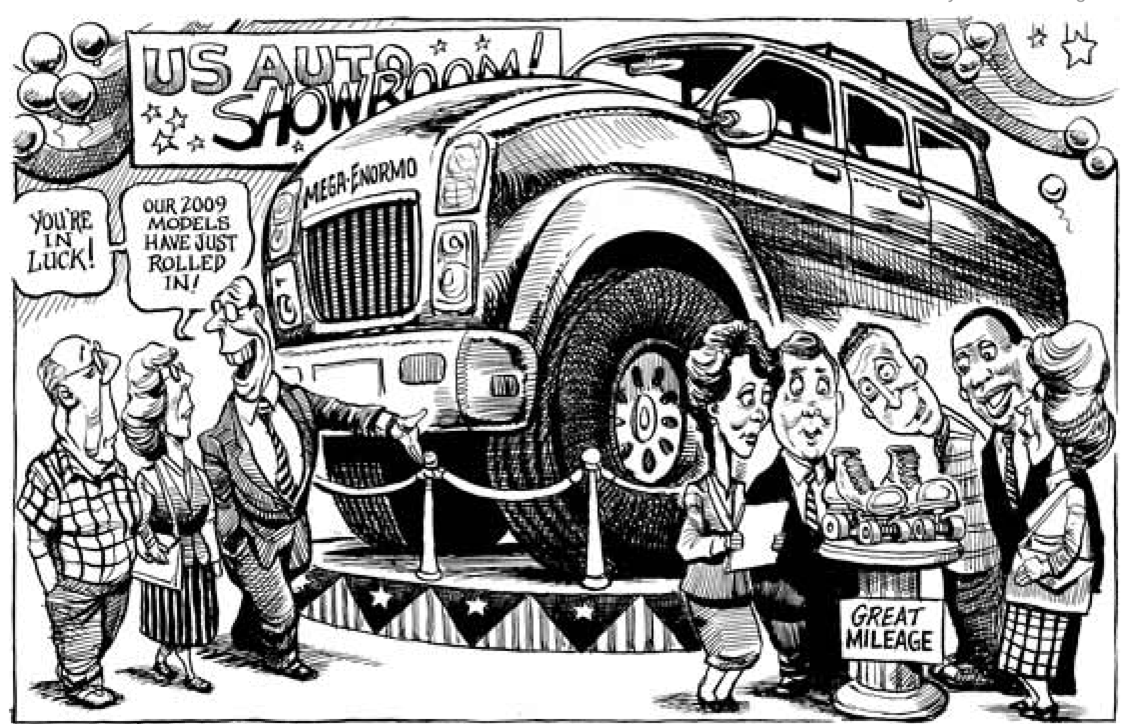
America's United Steelworkers signed a partnership agreement with Britain's Unite, forming the first **transatlantic union**. American and British unions have been consolidating in their respective countries to counter falling membership; steelworkers, for example, only account for 20% of United Steelworkers members, with health-care workers, miners and others making up the rest. The unions now want to forge global alliances so as to bargain better with multinational companies.

The misery continued for **carmakers** in America. Sales in June were down by around a fifth, compared with the same month last year, at General Motors and Toyota, and by 28% at Ford. Chrysler's sales fell by 36%, giving it less than 10% of the overall market. See article

KAL's cartoon

Jul 3rd 2008
From The Economist print edition

Illustration by Kevin Kallaugher

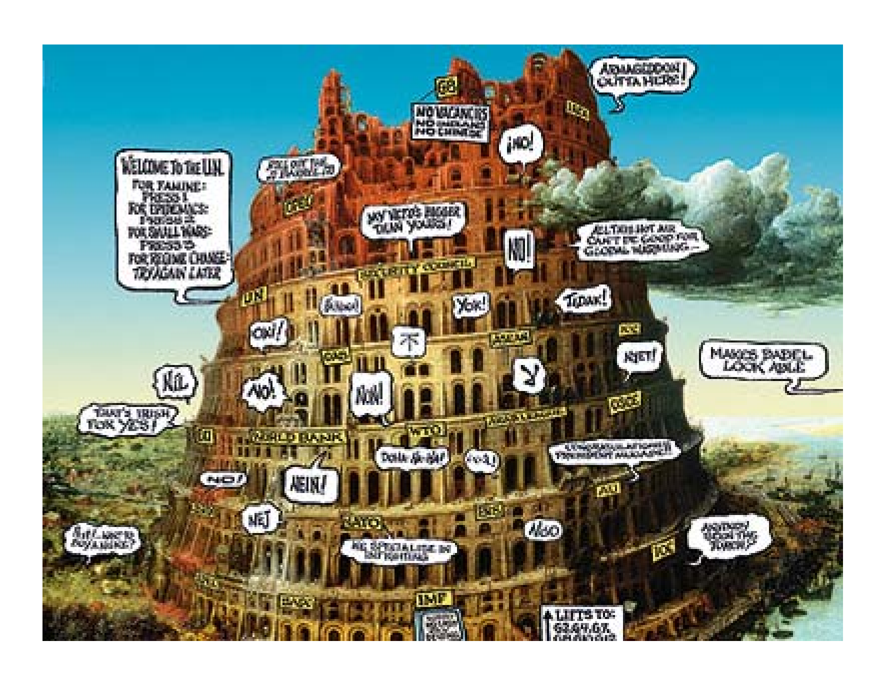


What a way to run the world

Jul 3rd 2008
From The Economist print edition

Global institutions are an outdated muddle; the rise of Asia makes their reform a priority for the West



CLUBS are all too often full of people prattling on about things they no longer know about. On July 7th the leaders of the group that allegedly runs the world—the G7 democracies plus Russia—gather in Japan to review the world economy. But what is the point of their discussing the oil price without Saudi Arabia, the world's biggest producer? Or waffling about the dollar without China, which holds so many American Treasury bills? Or slapping sanctions on Robert Mugabe, with no African present? Or talking about global warming, AIDS or inflation without anybody from the emerging world? Cigar smoke and ignorance are in the air.

The G8 is not the only global club that looks old and impotent (see article). The UN Security Council has told Iran to stop enriching uranium, without much effect. The nuclear non-proliferation regime is in tatters. The International Monetary Fund (IMF), the fireman in previous financial crises, has been a bystander during the credit crunch. The World Trade Organisation's Doha round is stuck. Of course, some bodies, such as the venerable Bank for International Settlements (see article), still do a fine job. But as global problems proliferate and information whips round the world ever faster, the organisational response looks ever shabbier, slower and feebler. The world's governing bodies need to change.

Time for a cull?

There has always been an excuse for putting off reform. For a long time it was the cold war; more recently, "the unipolar moment" convinced neoconservatives that America could run things alone. But now calls for change are coming thick and fast. Britain's prime minister, Gordon Brown, and America's treasury secretary, Hank Paulson, want to redesign global financial regulation. Others are looking at starting afresh: John McCain is promoting a League of Democracies, while Asian countries are setting up clubs of their own—there is even talk of an Asian Union to match the European one. And many critics, especially in America, want a cull. Surely economic progress in the emerging world argues for getting rid of the World Bank? Is a divided Security Council really any use?

The critics are right to argue that global organisations should be more focused than they are, but wrong to assume they can be dispensed with altogether. Get rid of the Security Council or the World Bank and the clamour to invent something similar would begin: you need somebody to boss around 100,000 peacekeepers and to lend to countries that find it hard to access capital markets. International talking-shops and standard-setters are here to stay; instead of trying to bin them, focus on making them work well.

That means recognising how economics has changed the world order. Emerging economies now account for more than half of global growth. The most powerful among them need to be given a bigger say in international institutions—unless of course you think India will always be happy outside the Security Council and China content to have a smaller voting share than the Benelux countries do at the IMF.

Any solution must accept three constraints. First, better institutions will not solve intractable problems. A larger G8 will not automatically lick inflation, a better World Food Programme would not stop hunger. Second, no matter how you reform the clubs' membership rules, somebody somewhere will feel left out. Third, you cannot start again. In 1945 the UN's founders had a clean slate to write upon, because everything had been destroyed. The modern age does not have that dubious luxury, so must build on what already exists.

Take for instance the G8. Some dream of reducing it to just the economic superpowers: the United States, the EU, China and Japan. An appealing idea, but Silvio Berlusconi and Vladimir Putin are unlikely to give up their seats at the top table. Better to enlarge the current body to include the world's biggest dozen economies. A G12 would bring India, Brazil, China and Spain into the club, while allowing Canada (just) to stay in.

The politics of the Security Council are even more outdated. Nobody now would give France or Britain a permanent veto, but neither wants to give up that right. Meanwhile, the four obvious candidates are held back by regional jealousies: India by Pakistan; Brazil by Argentina; Germany by Italy; and Japan by China. The most sensible plan gives these four permanent but non-veto-wielding seats, with two other seats provided for Islamic countries and one for an African nation.

America has yet to get behind these proposals, but a sharpened Security Council could mitigate the emerging world's objections to UN reform. With a more representative high command, more jobs could be allocated on merit, the globocracy slimmed and bolder steps considered: for instance, the case for a small standing army, or earmarked forces, to nip Darfur-style catastrophes in the bud, would be easier to make.

The Bretton Woods duo are easier to change: all that is needed is Western will. Their problem is finding a useful purpose. The World Bank is still needed as a donor to the really poor and as a supporter of global public goods, such as climate-change projects. There is less obvious need for the IMF, which was originally set up to monitor exchange rates. It could become a committee of oversight, but the main financial regulation will stay at the national level.

League of Good Hope

Supporters of Mr McCain's League of Democracies suggest it could be like NATO—a useful democratic subcommittee in the global club. But Mr McCain needs to define his democracies. (Will Malaysia count? How about Russia or Iran?) And, crucially, any league must not be seen as an alternative to reforming the UN. The whole point of global talking-shops is that they include everybody, not just your friends.

Faced with the need to reform international institutions, the rich world—and America in particular—has a choice. Cling to power, and China and India will form their own clubs, focused on their own interests and problems. Cede power and bind them in, and interests and problems are shared. Now that would be a decent way to run a world.




The credit crunch

Britain's sinking economy

Jul 3rd 2008
From The Economist print edition

It is going to get nasty; exactly how bad depends on the Bank of England and, especially, Gordon Brown

Getty Images



THE portents are increasingly gloomy. More and more signs are pointing to a punishing slowdown—with a recession looking likelier by the day. After 16 years in which Britain's GDP has grown without halt, a downturn will come as a painful shock. Yet what may matter more is how Gordon Brown's enfeebled government responds to the bad times ahead.

A stream of unwelcome news has reinforced fears that the British economy, still the fifth-largest in the world in 2007, is set to shrink. Those concerns were crystallised on July 2nd when two large firms reported serious setbacks. Taylor Wimpey, the country's biggest homebuilder, revealed that it had been unable to raise the extra finance it needs to shore up its balance-sheet. Marks & Spencer, a food and clothing retailer, reported falling sales and Stuart Rose, its chief executive, gave warning of "stormy times ahead". Both companies' shares, especially Taylor Wimpey's, tumbled heavily in subsequent trading, and the pound also fell in response as foreign-exchange dealers became more fretful about Britain's prospects.

The markets are pinpointing two areas in which the economy is most vulnerable to a downturn: housing and retailing. Just as America's growth has been dragged down since 2006 by falling residential investment, so Britain is now suffering a sharp contraction in homebuilding. That forms part of a broader slump in the housing market, in which turnover is shrinking because mortgage finance has dried up and house prices are tumbling (see article). Households are already being squeezed by the soaring costs of fuel and food. Now they are feeling even poorer as their homes fall in value, which makes them reluctant to shop.

Official figures, it has to be said, paint a more uplifting picture. The national accounts show GDP grew at an annual rate of 1.1% in the first quarter, a modest pace compared with the trend rate of 2.5-2.7% but some way from recession. Yet business surveys are signalling a downturn. Consumer confidence is at an 18-year low; for big purchases it has plumbed a 26-year low. And even if the official numbers turn out to be right, the prospects for both GDP growth and consumer spending look dire as living standards stagnate because of rising inflation.

Not just recession, M&S recession

Maybe the British economy will muddle its way through over the next year or two without going into

recession; but it would be surprising if it did. Like other rich countries, Britain is feeling the downdraft from the credit crisis at a time when rising inflation makes it hard for the central bank to provide succour. But it is more exposed than most for three main reasons.

First and foremost, the housing bubble was one of the frothiest in the world. Real house prices increased by around 140% in the ten years to early 2007. In Spain (see article) and Ireland, where price gains rivalled Britain's, heady housing-market booms have given way to bust. House prices in America are falling faster than during the Great Depression.

Second, British households are the most indebted in the G7, and the tide of cheap credit that caused the housing and consumer-spending booms has ebbed particularly fast in Britain. Within Europe, British mortgage lenders were especially keen on securitising home loans (pooling them to back bonds sold on to investors). The virtual closure of the securitisation market over the past nine months has thus had a disproportionately big effect on mortgage finance in Britain.

Third, economic growth was buoyed in recent years as the City thrived on the back of all the clever financial deals that have now come unstuck. An economy that came to rely as heavily as Britain's did on finance is clearly vulnerable to an extended banking crisis. The era in which GDP growth was supercharged by a financial-sector boom is over.

From hubris to humility

Adapting to this new world will be hard. Business tycoons who grew rich on cheap, sound money will need new skills; so will David Cameron's Conservatives, whose focus has been on social policy, not economics. But for Mr Brown, a stumbling economy will be an especially chastening experience.

When he was chancellor of the exchequer, inflation was low and stable, national output grew quarter after quarter, and year after year Mr Brown boasted of his brilliant management. Now his claims look hubristic. Indeed, public fears about the economy are the main reason why the Tories have surged in the polls. Having made his economic reputation in fair weather, Mr Brown must now cope with more troubled times.

Two temptations present themselves. One will be to mount a fiscal rescue package. If Mr Brown had fattened the public finances during the good times, as he should have done, then this would be no bad thing. Unfortunately, he did quite the opposite. And now the Treasury has bent its supposedly binding fiscal rules by borrowing £2.7 billion ($5.4 billion) this year to help tax losers from Mr Brown's final budget. The government cannot afford more vote-pleasing handouts.

A further, and larger, worry concerns monetary policy. Siren voices are arguing for the Bank of England to cut interest rates again. It should ignore them. Consumer-price inflation is already at 3.3% and expected to rise above 4% (double the official target rate) later this year. Britain's economic prospects already look bad enough. Letting inflation escape would cause even more pain in the long run. The abiding lesson of monetary history is that the higher inflation gets, the costlier it becomes to bring down again.

Therein lies Mr Brown's second temptation. Making the Bank independent was one of his genuine achievements: he has no day-to-day control over it. But he could still influence outcomes by raising the inflation target and thus loosening monetary policy; and a government whose electoral prospects look as dire as this one's do is bound to be tempted.

If Mr Brown succumbs to that temptation, he might pick up a few more votes at the general election due within the next two years—but probably not enough to win. And he would then go down in history as a prime minister whose tenure was as disastrous as it was brief.

Colombia

Gracias and good night

Jul 3rd 2008
From The Economist print edition

Despite his coup in freeing Ingrid Betancourt, Álvaro Uribe should not seek a third term

AFP



ONLY those blinded by ideology would deny that Álvaro Uribe has made Colombia a better place. By expanding the security forces and leading them tirelessly, Mr Uribe, who was first elected president in 2002, has imposed the authority of the democratic state across most of a previously lawless country. He persuaded thousands of right-wing paramilitaries to disarm, and has inflicted probably mortal blows on the FARC guerrillas. The latest of these was the dramatic liberation this week of the FARC's most-prized hostages, including Ingrid Betancourt, a politician of Colombian and French nationality kidnapped six years ago, and three American defence contractors (see article). Murders have almost halved since 2002; kidnappings have fallen much more. A safer country is prospering economically, as confidence returns.

This record has won Mr Uribe his people's gratitude (opinion polls give him an approval rating of 80%) and in 2006 a second term—after he persuaded Congress to lift a constitutional ban on consecutive presidential terms, and the courts to ratify the change. But now this second term is unexpectedly in question. On June 26th the Supreme Court found that a former legislator cast a deciding committee vote for the re-election amendment only after two ministers had promised government jobs to some of her supporters. The justices have asked the Constitutional Court to rule on the legality of the constitutional change and thus of the 2006 election.

Mr Uribe's reaction was characteristically combative. He asked Congress to call a referendum on the legitimacy of his term. He claims that the courts are pursuing a political vendetta. He has a point: reprehensible though it is, patronage politics is routine in Colombia and much of the democratic world. To deduce that in this case it invalidates the election is disproportionate—as the Constitutional Court may well conclude.

But the president's referendum idea is equally cock-eyed. He seems determined to battle the courts, rather than respect them. Worse, although he has denied this, the referendum suggests to many a step towards prolonging his rule beyond 2010. He has allowed supporters to gather signatures for a (separate) referendum to change the constitution again to allow him a third term. This would give him time to finish off the FARC and complete his rescue of Colombia, supporters say.

He deserves a full second term—but no more

Tempting though such a prospect might seem, a third term would be disastrous for Colombia. Mr Uribe is not without flaws. Worryingly, given his feud with the judiciary, judges nominated by him will form a majority in the Constitutional Court by next year. His shoot-from-the-hip manner has made him many enemies abroad, including in America's Democratic Party. He may be welcoming John McCain to Colombia this week, but it is Barack Obama who is ahead in the opinion polls and the Democrats control

Congress (where they are disgracefully blocking a trade agreement with Colombia mainly because of their distaste for Mr Uribe). A different Colombian president might also carry out the agrarian reform—settling people displaced by violence on land confiscated from warlords—that Colombia needs and Mr Uribe eschews.

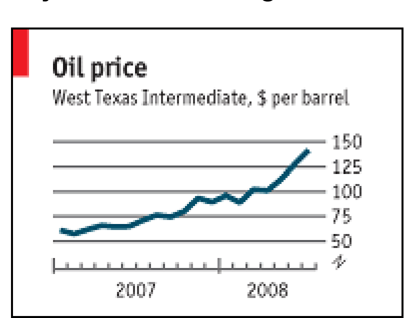
Most importantly, Colombia's transformation will remain fragile as long as it is the work of one man. To be complete, it needs to be institutionalised. There are several plausible successors who would maintain Mr Uribe's security policies. Rather than a plebiscitarian strongman, in the mould of Venezuela's Hugo Chávez or Peru's Alberto Fujimori, Colombia needs strengthened democratic institutions. The greatest service Mr Uribe could do his country is to depart in 2010.

The oil price

Don't blame the speculators

Jul 3rd 2008
From The Economist print edition

Politicians who try to make oil cheaper by restraining speculation will just make things worse



ALTHOUGH the price of oil continues to hit new records, it has in one respect been a quiet week on the oil markets. America's lawmakers are celebrating Independence Day by taking a few days off. That has led to a brief interruption in the torrent of proposals aimed at curbing speculation.

Ten different bills on the subject are in the works in Congress. Before the House of Representatives shut up shop, it approved one by a vote of 402-19. America's politicians are not the only ones to have fingered speculators for the feverish rise in the price of oil and other raw materials. Italy's finance minister believes that there is a "magnum of speculative champagne" included in the price of each barrel. Austria wants the European Union to impose a tax on speculation. Saudi Arabia and other big oil producers routinely blame the price on frothy markets, rather than idle wells.

The accusers point to the link between the volume of transactions on the futures markets and the price of oil. Since 2004 the near tripling of trading in oil on the New York Mercantile Exchange (NYMEX), the world's biggest market for the stuff, has neatly coincided with a tripling in the price.

What is more, investing in oil has become something of a fad. Commodities traders and hedge funds with long experience have been joined by less expert sorts, including pension funds and individuals. All this, the theory runs, is contributing to a bubble in commodities. The rush of punters betting on higher prices is begetting a self-fulfilling prophecy: it is the tide of new investment, rather than inadequate supply or irrepressible demand, that is pushing the price of oil ever higher.

Follow the oil, not the futures

This reasoning holds obvious appeal for those looking for a scapegoat. But there is little evidence to support it. For one thing, the surge in investment in oil futures is not that large relative to the global trade in oil. Barclays Capital, an investment bank, calculates that "index funds", which have especially exercised the politicians because they always bet on rising prices, account for only 12% of the outstanding contracts on NYMEX and have a value equivalent to just 2% of the world's yearly oil consumption.

More importantly, neither index funds nor other speculators ever buy any physical oil. Instead, they buy futures and options which they settle with a cash payment when they fall due. In essence, these are bets on which way the oil price will move. Since the real currency of such contracts is cash, rather than barrels of crude, there is no limit to the number of bets that can be made. And since no oil is ever held back from the market, these bets do not affect the price of oil any more than bets on a football match affect the result.

The market for nickel provides a good illustration of this. Speculative investment in the metal has been growing steadily over the past year, yet its price has fallen by half. By the same token, the prices of several commodities that are not traded on any exchanges, such as iron ore and rice, have been rising almost as fast as that of oil.

Speculators do play an important role in setting the price of oil and other raw materials. But they do so based on their expectations of future trends in supply and demand, not on whims. If they had somehow managed to push prices to unjustified heights, then demand would contract, leaving unsold pools of oil.

The futures market does sometimes signal that prices are likely to rise, which might prompt speculators

to hoard oil in anticipation. But it is not signalling that at the moment, and there is no sign of hoarding. In the absence of rising stocks, it is hard to argue that the oil markets have lost their grip on reality.

Some claim that oil producers are in effect hoarding oil below the ground. But there is also little sign of that, either among companies or countries: all big exporters bar Saudi Arabia are pumping as fast as they can.

It takes two to contango

Despite their dismal reputation, the oil speculators provide a vital service. They help airlines and other big oil consumers to hedge against rising prices, and so to reduce risk—a massive boon amid the economic turmoil. By the same token, they provide oil producers with more predictable future revenues, and so allow them to expand more confidently and borrow more cheaply. That, in turn, should help to lower the price of oil in the long run. Any attempt to curtail speculation, by contrast, is likely to make life harder for firms and oil more expensive.




Malaysia

South-East Asia's Gorbachev?

Jul 3rd 2008
From The Economist print edition

Abdullah Badawi certainly does not deserve that title. With boldness, he could yet do so

AP



DEFENDERS of Malaysia's prime minister, Abdullah Badawi, liken him to Mikhail Gorbachev: a statesman who emerged from deep inside a declining, dysfunctional system and yet had the courage to carry out risky but badly needed political reforms. With Malaysians squabbling viciously over improbable new allegations against the opposition leader, Anwar Ibrahim, and Mr Badawi's own heir-apparent, Najib Razak, the system has never looked in more need of a reforming hero (see article). But is Mr Badawi, who succeeded Mahathir Mohamad in 2003, really up to it?

His premiership has already had several twists and turns. At first, Mr Badawi's laconic, laid-back style came as something of a relief after 22 long years of the combative Dr Mahathir. Soon, however, drift and decadence took over. That in turn helped bring a stunning electoral setback in March: the ruling coalition saw its majority slashed.

This was exciting in itself, because Malaysia has been, in effect, under one-party rule since independence from Britain in 1957. Mr Badawi's United Malays National Organisation (UMNO), which dominates the ruling coalition, is probably, proportional to the population, the world's biggest mass party, with more than 3m members, mostly Malays (just over half the country's 25m people). More encouraging still, Mr Anwar's supporters campaigned against the institutionalised racism of UMNO's pro-Malay affirmative action policies and many voters agreed these policies had become a vehicle for corrupt patronage. It was not just ethnic-Chinese and Indian voters who deserted the government. So did many Malays.

But the election was also thrilling because the result (and Mr Anwar's attempts to lure away Mr Badawi's supporters since) have prodded the prime minister into new political boldness. Mr Badawi has started to clean up the legal system and repair some of the damage done to the independence of the country's judiciary. Mr Badawi has also taken the risky decision to cut fuel subsidies, sending petrol prices soaring. The Gorbachev comparisons spring from these past few months.

The new Malay dilemma

Yet there are two problems with Malaysian *glasnost*. The immediate one is the scandals, which are depressingly like Malaysian politics as usual—only more so. Just as in 1998, Mr Anwar faces a charge of sodomy, a criminal offence in Malaysia. Now as then, he denies the charge (which on the previous occasion was eventually thrown out) and accuses the government of organising a smear campaign. Indeed he has said his accuser is closely linked to Mr Najib. The latter faces even more damaging

questions about the murder of a female Mongolian translator: his political adviser is one of those charged.

The second, deeper problem is that the Gorbachev comparison is, on closer inspection, hardly comforting for Mr Badawi. The former Soviet leader thought he was reviving a system that still had some life in it. In fact it had to be destroyed so something new could be erected in its place (so Mr Gorbachev gets credit for managing the inexorable decline of a political system in a relatively peaceful way).

Malaysia is not in such a terminal mess. Compared with the old Soviet Union's, its economy is a picture of vitality. Nor is it a totalitarian state; by Soviet standards it is an amicable federation. Its problem is that like other places where one party is so dominant, politics has become ossified and corrupt. It could still be reformed without having to start from scratch; but a lot depends on what Mr Badawi does now.

For Mr Badawi does indeed face a Gorbachev-style choice. He could try to shore up the old system. By discrediting the opposition and using the usual perks, threats and blandishments of incumbency, UMNO and its partners could yet cling to office, at least for a while. Or Mr Badawi could embrace reform, clean the system up and compete for power without the dirty tactics. If he does, he will indeed deserve an honourable mention in the history books.

In March Malaysian politics entered a new era. A transfer of political power, until then a remote possibility, has since begun to seem an inevitability—if not as soon as Mr Anwar would like. Whatever Mr Badawi's merits or faults, preserving internal peace during such an unprecedented transition will take more than one man; the whole political class, including Mr Anwar, will have to share responsibility. Neither side is immune from a big populist temptation: to play on the fears of the Muslim Malay majority and convince them that their traditional privileges are at risk. At a time when political Islam (including some quite extreme strains of that ideology) is on the march, that could be disastrous.

The presidential campaign

Return to centre

Jul 3rd 2008
From The Economist print edition

John McCain is veering off to the right—and making things too easy for Barack Obama

AP



WHEN more than 80% of Americans tell pollsters that they think the country is on the wrong track, and when only 28% of them believe that the president is doing a good job, you don't need a Karl Rove or a Dick Morris to tell you that the road to the White House involves steering well clear of the incumbent's policies. So why is John McCain not doing it?

The Republican candidate has always been close to George Bush when it comes to defending two fundamental, if unpopular, points of principle—the Iraq war and free trade. But in recent months Mr McCain has slid to the right on a series of other issues, including tax cuts, offshore drilling, immigration and even torture. This manoeuvring seems insincere and short-sighted.

Sincerity is important with Mr McCain. He has been at his most attractive, especially to independents such as this newspaper, when he stands up for issues that he believes in. On the Iraq war, his position has been almost Churchillian: victory at all costs, victory in spite of all terror. Declaring that he would rather lose an election than a war is paradoxically one of the Republican candidate's most valuable electoral assets. It makes him sound like a commander-in-chief.

The same goes for Mr McCain's support for free-trade agreements. Only a third of the country thinks these are good for America, the lowest figure, alas, in the developed world. But Mr McCain's position has been clear, consistent and right. As with Iraq, it is his opponent, Barack Obama, who is having to track towards the centre, trying to renounce some of the crowd-pleasing claptrap he uttered in the primaries.

That this newspaper admires Mr McCain for taking positions it agrees with may seem hardly surprising. Yet he still maintains some of his allure when he takes the wrong course, but does so plainly out of principle. His support for the embargo on Cuba and his opposition to gun control at home may be wrong-headed, but they are genuine. His League of Democracies and his overheated rhetoric about Iran are misguided, but they are consistent with his political history. In a world short of conviction politicians, Mr McCain's Straight Talk Express has its charms.

But not when the straight talker starts saying things it is very hard to imagine that he remotely believes in. It was a bad omen last year when this freewheeling western conservative in the Reagan mould went off to court the intolerant Christian right. And recently, the flip-flops have come rapidly. Once a vigorous opponent of Mr Bush's tax cuts, he says he wants not only to continue but also to extend them. Once a champion of greenery, he has called not only for an expensive petrol-tax holiday (something Mr Obama cleverly resisted) but also for a resumption of drilling off America's coast. Once a supporter of closing down Guantánamo Bay, he recently criticised the Supreme Court for daring to suggest that inmates

deserve the right of habeas corpus. He has edged to the right on two other areas where he used to be hated by his party's conservatives as a dangerous maverick: on torture (he won't rule out water-boarding) and immigration reform (he says fix the border first, which will take an eternity).

Don't be spooked, John

It is true that America still has more conservatives than liberals. But the Republican Party has known for a long time that Mr McCain is not precisely one of them—and they still chose him anyway. Conservatives were smart enough to see that his appeal to independents and floating voters, who make up a larger proportion of the electorate than either of the two main parties, is their only hope of retaining the White House.

American elections classically involve a two-step: the candidate runs to the extreme in the primary, then back to the centre for the general. Mr Obama is doing that. Mr McCain seems to be doing precisely the opposite. It is a mistake.



On the Lisbon treaty, American politics, the Roma, biofuels, green taxes, Poland and Russia, circumcision

Jul 3rd 2008
From The Economist print edition

Europe's treaty conundrum

SIR – With regards to the rejection by Irish voters of the European Union's Lisbon treaty, you argue that it is "stupefyingly arrogant and anti-democratic to refuse to take no for an answer" ("Just bury it", June 21st). I put it to you that little could be so stupefyingly arrogant and anti-democratic as wishing to deny to the Irish government, on a matter that is entirely between it and the Irish people, the right to see whether the reasons why many Irish voters said no can be resolved.

If their government decides the issues can be resolved, then how can it possibly be "contemptuous of democracy" for the treaty to go back to the Irish people? It is surely contemptuous to seek to deny them this possibility. What do you think you are doing, telling the Irish what to do while arguing that member-state governments may not make their own views known?

You unwittingly gave away an important point in arguing that the changes in the treaty, ie, sorting out a muddle in foreign policy and a fairer system of voting in the EU, "are not the sorts of changes to set voters alight", and therefore by implication should not be made. This is a counsel of despair, since it means that anything that does not excite the voter (which, let's be candid, is most things in the EU), even if highly desirable but requiring treaty change, cannot be done. You cannot really mean that, yet it is the consequence of your line of thinking.

Sir Brian Crowe
London

SIR – I am shocked by the Franco-German response to the result of the Irish vote. Trying to isolate and intimidate a small country is not the proper foundation for the formation of a new superpower. France seems to think that as the Irish are a small nation they are less important than the French. When the French and Dutch rejected the constitution in 2005, nobody supported a strategy to isolate and intimidate them into bypassing the popular vote.

Furthermore, it is shameful that other European governments did not hold their own referendums. If they are so sure of the treaty's merits then they should be capable of selling it to their people. Their tactics regarding the treaty merely nurture anti-EU sentiments and drive more people towards taking a Eurosceptic position.

Brian Fleming
Anchorage, Alaska

SIR – While I agree that there are "more urgent matters" for the EU to deal with than institutional reform, the Lisbon treaty was at least an attempt by government leaders finally to get the lengthy debate on a constitution off the table in order to focus on real world problems. This probably explains their anger over the Irish vote, which drags the union back into endless discussions.

Moreover, the treaty would have reorganised, strengthened and brought some necessary coherence to foreign-policy making in the EU, and therefore helped the member states formulate policy on energy, climate change, immigration, dealing with Russia, enlargement and other issues you mentioned as important.

Hylke Dijkstra
Maastricht, the Netherlands

SIR – We should not accept that the Lisbon treaty is dead. Those countries that do not want to be part of

a strong Europe should move out of the way. Lucien Febvre, a French historian, noted in his 1945 work, “L’Europe: Génese d’une civilisation”, that the modern notion of Europe was born with the Carolingian empire, and that Europe’s heart is France, Germany, northern Italy and the Low Countries: in other words the founding members of the EU.

The way out of this politician-created mess is the re-foundation of the EU, with a new heart composed of those countries wishing for a stronger union moving forward, and the others staying behind. The EU constitution could then be discussed and accepted by countries before they join.

Pedro Santos
Estoril, Portugal

The state of the union

SIR – Your article on the political self-segregation of Americans in towns and counties may have identified a demographic trend, but it is wrong to view that trend as the cause of America’s increasingly strident national politics (“The Big Sort”, June 21st). Indeed, the constitution recognises that different communities will have diverse priorities and elegantly solves the problem with federalism, leaving powers not prescribed to the national government to the states. People can choose to live in states and towns that best reflect their values.

Unfortunately, the federal government has spent the past few decades assuming more and more power over issues that should be handled by state and local governments. At the same time, federal courts have interfered in decisions that are best left to the states. So yes, politics has become more bitter and polarised, but the problem isn’t American tribalism. The rancour has increased because whichever political party controls the national government now has broader powers to force its ideological agenda on local communities.

Mark Weber
Overland Park, Kansas

SIR – Could it be that the political clustering of Americans is a function of the electoral system? The United States is made up of single-member districts where a simple majority wins a congressional seat and the loser gets nothing.

If an American identifies strongly with Republican or Democratic values it is surely rational for him to move to a district he knows will return his preferred candidate. As more like-minded people move to the area, then it is no surprise that the number of “landslide counties” should increase over time. Other countries with similar electoral arrangements, like Britain, should take heed.

Taggart Davis
Colchester, Essex

SIR – Your noteworthy powers of observation seem to have failed you when describing the suburbs of Washington, DC. The suburbs located in Maryland may tend to be more liberal by comparison, but northern Virginia is certainly not a bastion of conservatism. We elect Democrats to Congress (such as Jim Moran of Alexandria), and the Republicans we vote for are moderates. People moved here because of the schools, the low crime rate, the job opportunities and a business-friendly environment. I don’t know anyone who chose to live in northern Virginia because it is more conservative than Maryland. Move south across the Rappahannock River towards Richmond, however, and it’s a different story.

Bob Johnson
Burke, Virginia

SIR – I live in Arlington, which is nicknamed by some as “The People’s Republic of Arlington” because of its liberal tendencies. There may be pockets of wealthy conservatives in northern Virginia, but it is certainly not the norm. During the primaries Hillary Clinton came to speak at my school because she has a strong base here.

Mary Beech
Arlington, Virginia

SIR – The political segregation of Americans usually carries abroad, with a consequence that many are reluctant to talk about sensitive topics when travelling. The real world is too troublesome to discuss with relative strangers and so we talk about our grandchildren. Not so with other English-speaking nations. After several vacations in Europe, I found that the best company at dinner came from Canadians or the British. Canadians especially can and will discuss anything with anybody.

Keith Baker
Heber City, Utah

How best to help the Roma

SIR – Your briefing on Europe's Roma accurately depicts the attempts by that minority to achieve equal status in society as a failure ("Bottom of the heap", June 21st). For the Roma themselves, the main challenge at the moment is to become better organised in order to fight more effectively for their rights. This has so far proved a difficult task because of a number of factors, including the habit of the authorities to support less capable Roma who are more easily manipulated, and even the apathy of the Roma themselves who are accustomed to receiving assistance from outsiders.

Despite its shortcomings, the role of the much maligned "Romany elite" is crucial at a time when Roma are increasingly becoming the scapegoats of Europe. The way in which funders have invested in the present Roma elite is indeed questionable. A Romany elite who can speak loudly about the blatant violations of Roma rights is of the utmost urgency and needs encouragement.

Marcel Dediu
Spolu International Foundation
Utrecht, the Netherlands

Valeriu Nicolae
Executive director
European Roma Grassroots Organisations (ERGO) network
Bucharest

Constantin Cojocariu
Lawyer
London

David Mark
Lobbyist
Brussels

Biofuels and advertising

SIR – A full-page advertisement from Abengoa Bioenergy that ran in the British and European editions of your June 21st issue stated that, "Bioethanol is currently the only real alternative for eliminating our addiction to oil", and cited our 2004 report, "Greenhouse-gas emissions from transport in the EU25", as one of two sources to justify that claim. That they could misuse our name and research in an advertisement claiming to separate manipulation from evidence is reprehensible.

It would be impossible for a reader of our report to reach the conclusion that Abengoa draws. It doesn't even mention biofuels or bioethanol. If the company had any genuine interest in "supported evidence", as they claim, they would know that our view on biofuels bears no resemblance to their own.

We have consistently warned against volume targets for biofuels since at least 2004 when we published another report, "Sense and sustainability". We believe Europe should set an environmental target to cut greenhouse-gas emissions from the production of all transport fuels, not a biofuels quantity target that gives a boost to the fuels Abengoa produces, regardless of their environmental performance. Running Europe's fleet of heavy, gas-guzzling cars on biofuels rather than petrol is no cure. If Europe truly wants to end its addiction to oil, it should start by making cars twice as fuel-efficient as they are today. As an environmental group, our main capital is our reputation and credibility, which we will defend.

Jos Dings
Director
European Federation for Transport and Environment
Brussels

Green consumer-taxes

SIR – If a society decides to proactively reduce its total carbon emissions it makes little sense just to focus on the carbon it directly produces (Economics focus, June 21st). For example, a study by Dieter Helm of Oxford University shows that although greenhouse gases emitted directly in Britain had fallen by 15% since 1990 measured by the conventional method, "on a consumption basis, the illustrative outcome is a rise in emissions of 19% over the same period" and that "trade may have displaced" Britain's "greenhouse-gas appetite elsewhere".

Whether trade displacement is caused by variances in carbon regulations among countries, which you focused on, or other factors is less relevant than the total amount of carbon that was emitted to produce the goods and services consumed in a single country. As such, plans to introduce a "carbon tariff" on goods imported from countries such as China misses the point. Consumers are responsible for the goods they consume and the carbon emitted to produce them.

Emissions regulations have so far been aimed solely at the production of greenhouse gases, but governments tax goods and services at the point of production and consumption. It would therefore be more sensible to introduce an emissions "sales tax" rather than a carbon tariff.

Salman Farmanfarmaian
Geneva

Polish-Russian diplomacy

SIR – In response to your article on lingering Polish-Russian tensions over the Katyn massacre in 1940 ("Dead leaves in the wind", June 21st) I would say that such issues require courage and responsibility from politicians and historians trying to resolve them. This is particularly true when definitively explaining all the circumstances related to the Katyn massacre, and thus in preparing appropriate political solutions. An essential goal of the recently established Polish-Russian Group for Difficult Matters is to create a solid foundation for a partnership based on truth and mutual respect.

Adam Daniel Rotfeld
Co-chairman of the Polish-Russian Group for Difficult Matters
Warsaw

Snip away

SIR – There are two simpler rationales behind circumcision to the ones you mentioned: marking the tribe and hygiene ("Cutting the competition", June 21st). Clipping foreskins certainly reduces the ability of outsiders to feign membership or kinship. Removal of the foreskin also reduces the likelihood of acquiring and keeping some sexually transmitted infections (STI), which means fewer problems with female sterility.

As for circumcision's clear role in reducing the risk of HIV infection "for men", why are foreign governments keener to fund programmes for surgical procedures, when rolling out reliable hygiene infrastructure and improving access to STI prevention and treatment would provide similar results? No one seems to argue that European gay men should undergo the knife. In fact the success of social-marketing programmes in HIV prevention among gay men in the West underscores that there are effective alternatives.

John Egan
Vancouver

SIR – I deride your description of medical circumcision as "mutilation". Circumcision is an occasionally

necessary surgery, with verifiable, albeit usually negligible, benefits. Next you'll be saying that ear piercing or having droopy eyelids raised is "mutilation".

You also seem bewildered by the fact that the "fad" of infant circumcision is still widely practised in America. You have forgotten that there is a legitimate difference of opinion among doctors with regard to the merits of circumcision. Because no consensus has been reached, the American Academy of Paediatrics arrived at the nuanced position that the benefits of circumcision are not sufficient to recommend that all infant boys be circumcised.

The tradition of circumcision is a difficult topic existing at the nexus of religion and penises, two subjects about which humanity is prone to be particularly irrational.

Justin Kalm
San Diego

Economist.com BRIEFINGS

Who runs the world?

Wrestling for influence

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The post-war global institutions have largely worked well. But rising countries and growing threats are challenging their pre-eminence

THE powerful, like the victorious, do not just write history. They grab the seats at the top tables, from the United Nations Security Council to the boards of the big international economic and financial institutions. They collude behind closed doors. They decide who can join their cosy clubs and expect the rest of the world to obey the instructions they hand down.

That is how many outsiders, not just in the poor world, will see the summit that takes place from July 7th to 9th of the G8, the closest the world has to an informal (ie, self-appointed) steering group. Leaders of seven of the world's richest democracies, plus oil-and gas-fired Russia, gather this year in Toyako, on Hokkaido in northern Japan, to ruminate on climate change, rising food and energy prices, and the best way to combat global scourges from disease to nuclear proliferation.

But in an age when people, money and goods move around as never before, this little group no longer commands the heights of the global economy and the world's financial system as the core G7 used to do when their small, purposeful gatherings of the democratic world's consenting capitalists first got going in the 1970s. Nowadays summits produce mostly lengthy communiqués and photo-opportunities. And Russia's slide from democracy into state-directed capitalism has lowered the club's political tone.

In an effort to show that the G8 is still up with the times, Japan, like Germany last year, has invited along for a brief chat leaders from five "outreach" countries: Brazil, China, India, Mexico and South Africa. Yet this handshake between those who did best out of the 20th century and some potential shapers of the 21st leaves hanging the question of how the old world order should be adapting to the new.

Might the world be better managed by such a G13? Or a G15 or G16, to include a couple of weighty Islamic states too? Or, to preserve the group's original globe-steering purpose, by a G12 of the world's biggest economies? Meanwhile, the global institutions set up after the second world war are also having to look hard at their own futures. Unlike the G7/8, which takes on a bit of everything, these institutions basically divide into two sorts: economic and financial, and political.

At the pinnacle of world political management, but looking increasingly anachronistic, is the UN Security Council. Of its 15 members, ten rotate at the whim of the various UN regional groupings. The other five, which wield vetoes and are permanent, are America, Russia, China, Britain and France, roughly speaking the victors of the last long-ago world war. Alongside them is a secretary-general (currently Ban Ki-Moon from South Korea; this job, too, tends to go by regional turn), a vast bureaucracy at UN headquarters in New York, and hundreds of specialised agencies and offshoots (see table).

Busy busy busy

	Year started	Number of staff	Budget, $bn, 2007*	What it does
Some of the UN programmes and funds				
UNCTAD	1964	450	0.1	Integration of developing countries into the world economy
UNEP	1972	890	0.2	Promotes the environment
UNICEF	1946	7,200	3.1	Assistance to children and mothers in developing countries
UNDP	1965	5,300	4.9	Helps countries in their economic development
UNHCR	1950	6,300	1.0	Protection of refugees and resolution of refugee problems
WFP	1963	10,600	3.0†	Food for emergency needs and economic development
Some of the specialised agencies				
ILO	1919	1,900	0.5	Rights at work and employment opportunities
FAO	1945	3,600	0.8	Food and agriculture including forestry and fisheries
UNESCO	1942	2,100	0.7	Education, science, culture and communication
WHO	1948	8,000	1.6	Co-ordinating health matters
World Bank‡	1944	10,000	26.8§	Technical advice, loans, credits and grants for poverty reduction and the improvement of living standards
IMF	1944	2,500	0.9	Monitoring countries' economic and financial development, lending for balance-of-payments difficulties
IFAD	1976	430	0.1	Rural poverty
UNIDO	1966	650	0.2	Promotes growth in small and medium enterprises
Related organisations				
WTO (GATT)	1948	625	0.2	Trade agreements, negotiations and disputes
IAEA	1957	2,200	0.3	Scientific and technical co-operation in nuclear technologies; nuclear safeguards and inspections
Other organisations				
OECD	1961	2,500	0.5	Analyses and forecasts economic development, research on trade, environment, agriculture, technology, taxation
BIS	1930	578	0.2	Co-operation among central banks, monetary and financial stability

Sources: Official documents; annual reports

*Regular budget and extrabudgetary resources †2005 ‡Includes IDA (low-income) and IBRD (middle-income) §FY07: administrative budget $2.1bn, commitments $24.7bn

The world had to be saved not just from another war, but from a repeat of the Great Depression of the 1930s. That job went to a clutch of institutions: the World Bank and the International Monetary Fund (IMF), jointly known as the Bretton Woods institutions after the place of their creation; the Organisation for Economic Co-operation and Development, a rich-country think-tank set up in 1961; the much older central bankers' Bank for International Settlements; and the World Trade Organisation (WTO, formerly the GATT).

They have been buttressed too by conventions, conferences, courts, declarations, dispute-mechanisms, special mandates and treaties governing everything from human rights to anti-dumping complaints. The whole elaborate architecture has had extra underpinning from strong regional organisations, such as the European Union, and less elaborate ones like the African Union and the various talking-shops of Latin America, the Arab world and Asia, as well as from steadying alliances, such as NATO. As a result, there has been no return to the disastrous global conflicts of the first half of the 20th century.

Yet that very success has become one of three powerful pressures to adjust the way the world is run, as new economic winners (and some new losers) demand a say. Pressure also stems from intensifying resentment and frustration. After ringing declarations on human rights and even the adoption by a UN world summit in 2005 of a "responsibility to protect" against genocide and crimes against humanity, the UN Security Council still finds itself unable to agree to do much to protect the people of Darfur, Zimbabwe, Myanmar and others from the murderous contempt of their rulers—just as in the 1990s the UN failed the genocide victims in Rwanda.

If the Security Council, with a charter of high principles at its back, shows such feebleness towards tyrants (or to those who cavalierly flout nuclear treaties), doesn't it deserve to be bypassed? John McCain, the Republican candidate for president of the United States, supports the creation of a new League of Democracies which, its boosters argue, would have not only the moral legitimacy but also the will to right the world's wrongs effectively.

The third impetus to rejig the way the world organises itself is a dawning realisation on the part of governments, rich and poor, that the biggest challenges shaping their future—climate change, the flaws and the forces of globalisation, the scramble for resources, state failure, mass terrorism, the spread of weapons of mass destruction—often need global, not just national or regional, solutions. The shift in 21st-century economic power alone is justification for rebalancing influence in the top clubs. Much harder to figure out is which bits of the global architecture need mere tweaking, which need retooling or replacing—and who should have the right to decide.

After decades of dividing the world into the rich and powerful West and the developing (or emerging) "rest", China's rapid growth and the economic dynamism of East Asia had led to talk of a new "Pacific" century well before the old "Atlantic" one had ended. On present trends, somewhere between 2025 and 2030 three of the world's four largest economies will be from Asia. China will just pip America to top the global league, with India and Japan, both determined but so far unsuccessful campaigners for permanent seats on the UN Security Council, following on (though Chinese and Indians will still be, on average, much poorer than Americans or Japanese).

Not unipolar but what?

Yet talk of an Asian century sounds quaint. Despite America's brief "unipolar moment" as its rival pole, the Soviet Union, collapsed, Russia has recovered to join a rising China, America, Europe and Japan in a new constellation of big powers that is based on far more than the old boot-and-rocket counts of the cold war. Bring India into the snapshot, and you capture 54% of the world's population and 70% of GDP. Whether the leaders of this multipolar world will rub along or bash elbows remains to be seen.

Globalisation's increasingly unfettered flow of information, technology, capital, goods, services and people has helped spread opportunity and influence far and wide. To re-emergent China and Russia, add not just India but Brazil (these four bracketed by Goldman Sachs in 2001 as the upcoming BRICs), Mexico, South Africa, Saudi Arabia, South Korea and Australia, to name just some of the new winners as money changes pockets and the world turns faster.

A modern map of power and influence should also include transformational tools such as the internet; manipulators from lobbying NGOs to terrorist groups; profit-takers such as global corporations and sovereign wealth funds; and unpredictable forces such as global financial flows. The principal characteristic of this world, argues Richard Haass of the Council on Foreign Relations in a recent *Foreign Affairs* article, is not multipolarity but "nonpolarity". Dozens of actors, exercising different kinds of power, vastly complicate the effort to find a better balance of influence and responsibility. But the excuse of complexity is no answer to the demand for equity.

Some clubs have proved more responsive than others. China got a new economic start simply by ditching Marx, Lenin and Mao. But its reformers were able to tap the liberal rules-based system codified in the rules of the IMF and the World Bank (and later the WTO) for ideas as well as cash. China rejoined the bank in 1980 (the Nationalist government on Taiwan had been a founder member) just as its reforms got under way. Ironically, Communist-run China has since been one of the system's biggest beneficiaries. But it is by no means the only one. Despite the latest stockmarket dips and credit squeezes, world income per head has increased by more over the past five years than during any other similar period on record.

The IMF and the World Bank, pragmatic institutions from the outset, have adapted already, in fits and starts. In April the IMF reformed the peculiar formula by which it allocates votes and financial contributions according to economic size, reserves and other measures (see chart). China's share of votes will increase to 3.81%, still far short of its weight in the world economy. Meanwhile, old power patterns still determine who holds the two top jobs: the bank is run by an American, the fund by a European. But a bigger problem for both organisations is relevance.

Until the late 1990s the IMF, monitor of exchange rates and lender of last resort to struggling governments, had plenty of work. But emerging economies, once its chief clients and source of earnings in repaid interest and loans, are these days often awash with their own cash. Earlier this year the IMF board voted

to cut staff and sell off about an eighth of its gold reserves (some 400 tonnes) to meet expected future funding shortfalls. With no obvious role in coping with the aftermath of the recent banking and stockmarket turbulence, its future role may be more as an expert economic adviser.

Some worry that the world may still need a lender of last resort. Critics think the fund's days should be numbered and its reserves put to better use for development. Still others muse that what is needed is a World Investment Organisation, to set basic rules and better track the huge and complex flows of cash that now wash around in hedge funds, sovereign wealth funds, banks and financial markets.

The World Bank has a more certain future, but still needs to retool. Competition has stiffened from private capital markets. Many governments that once needed the bank's help for dams, roads and other big projects are earning plenty from the sale of raw materials. Even in Africa, the readiness of China and India to spend liberally without strings in pursuit of oil and minerals means that the Sudans and the Congos can take the bank's cash and ignore the conditions attached.

Lenders and borrowers

Voting shares, % *(% of total loans outstanding)*

	IMF	World Bank IDA	World Bank IBRD
United States	17	13	16 *(0)*
Japan	6	10	8 *(0)*
Germany	6	7	4 *(0)*
Britain	5	5	4 *(0)*
France	5	4	4 *(0)*
China	4	2	3 *(12)*
Russia	3	0	3 *(5)*
India	2*	4*	3* *(7)*
Brazil	2†	3‡	4‡ *(10)*
Others	53	52	50 *(67)*

*Total for Bangladesh, Bhutan, India, Sri Lanka
†Total for Brazil, Colombia, Dominican Republic, Ecuador, Haiti, Panama, Philippines, Trinidad and Tobago
‡Total for Brazil, Colombia, Dominican Republic, Ecuador, Guyana, Haiti, Panama, Suriname, Trinidad and Tobago

Sources: IMF; World Bank

Yet the bank still has a role lending to unfashionable causes, or countries which donors neglect. It could also provide global public goods: funding energy-infrastructure and climate-change projects are two examples, agriculture another.

A bit too equal

While the bank and the fund are steered by their biggest shareholders, the WTO, though relying on a representative caucus of states to hammer out deals, belongs to all its members: India and Brazil, for example, are at the heart of the Doha round of trade talks. But egalitarianism can be a weakness as well as a strength.

Much admired, at least by government lawyers, are the 60,000 pages of jurisprudence that govern the workings of the WTO dispute mechanism, which has helped resolve many a trade spat. The WTO ensures that members do not discriminate among each other—the best deal they offer to anyone must be extended to everyone. This has helped level the playing field and expand world trade. Russia's is the only large economy still outside the WTO, and that is its choice.

Yet those wanting to join must strike deals with each of the existing members—now a daunting 152. Operating by consensus means that the Doha "development" round has bogged down in disputes between developed and developing countries over complex, reciprocal cuts in farm subsidies and tariff barriers. The prospects for moving on to services look dim. Slow progress has helped push many to forge bilateral or regional deals instead. And if the Doha round fails completely, the recriminations could run far and wide—threatening any attempt, for example, to get agreement between the developed and developing world on new mechanisms to deal with climate change.

Economic and financial power is to some extent up for bids by governments with a stake in the game, and trade rules are (arduously) negotiable. Yet the distribution of political power has proved stubbornly—debilitatingly—resistant to change.

Most bitterly contested is membership of the UN Security Council, which has the right (whether exclusively or not is hotly debated) to decide what constitutes a threat to world peace and security, and what to do about it. In the UN's other big decision-making institution, the General Assembly, all the world can have its say, and does. But here outsiders take their revenge: a caucus of mostly developing countries called the G77 (but these days comprising 130 members including China) tends to dominate and filibuster.

Might it assuage resentment and improve the council's authority and the UN's effectiveness if America, Britain, France Russia and China invited other permanent members to join them—and considered giving up their veto? When the P5, as they are called, first grabbed the most powerful slots, the UN had 51

members; decades of decolonisation and splintering self-determination later, it has 192. The obstacles to reform grow no smaller either.

Most recently a concerted effort by Brazil, Germany, India and Japan (a self-styled G4) to join the council's permanent movers and shakers was thwarted by a combination of foot-dragging, jealousy and stiff-arming. African countries failed to agree on which of their several aspirants should join the bid. Regional rivals—Argentina and Mexico, Italy, Indonesia, Pakistan and others—lobbied to block the front-runners. China made it clear it would veto Japan; America, in supporting only Japan, helped destroy its friend's chances.

New permanent members would broaden the regional balance. That could add authority and legitimacy to council decisions. Bringing in not only nuclear-armed India, but soft-powered Japan and the rest, would undercut the notion, perpetuated by the P5, that to be a winner you need first to crash the nuclear club.

But might the price of a larger, permanently more diverse council be more potential spanner-tossers and thus greater deadlock? The hope would be that once difficult outsiders got their feet permanently under the table, sharing the responsibility for managing the world would stop them protecting bad elements, as South Africa (currently a rotating member) has been doing with Zimbabwe, in part to defy the permanent five.

Prising the P5 from their vetoes might, however, have adverse effects. It was dependable veto power, ensuring their vital interests were never overridden, that kept America and Russia talking at the UN—and Nikita Khrushchev shoe-banging—through the darkest episodes of the cold war. Russia will not forget the mistake of the brief Soviet boycott of the council that led to force being authorised to repel North Korea at the start of the Korean war in 1950. China shows no sign of veto self-effacement, either.

But staying at the table does not guarantee agreement. The UN is deliberately an organisation of states, and states differ for reasons good and bad. George Bush went to war in Iraq without explicit backing from the Security Council (just as NATO went to war to end ethnic cleansing in Kosovo, despite Russia's certain veto had the issue come to a council vote). But the council's divisions on the most contentious issues have not prevented responsible stewardship elsewhere. A Security Council summit in 1992 agreed that the proliferation of weapons of mass destruction was a “threat to peace and security” to be dealt with forcibly if need be. After the attacks of September 11th 2001, new resolutions were passed to curb terrorists' finance and keep nuclear, chemical and biological weapons out of their hands.

There has been a huge increase over the past 15 years in the numbers of blue helmets, with 100,000 soldiers and police currently deployed. This is credited with helping to reduce the number of conflicts between states, as well as calming civil wars from Bosnia to Haiti, from Cambodia to Sudan, from Congo to Lebanon. Acceptance, at least politically, of a “responsibility to protect” takes the council towards territory which, earlier this decade, it would not have approached: an International Criminal Court, for example, separate from the UN but able to take its referrals, and ready to prosecute the worst crimes.

Yet divisions among the P5 have often slowed deployment of peacekeepers where they are most needed, such as in Sudan's war-torn province of Darfur. Pessimists doubt that China and Russia, both arch-defenders of the Westphalian principle that state sovereignty trumps all, will ever seriously contemplate authorising forceful intervention even to end a genocide. A new UN Human Rights Council has yet to prove it is any better than its discredited predecessor at bringing brutal governments to book.

Meanwhile it took years, and North Korea's 2006 bomb test, for China to condemn Kim Jong Il's nuclear cheating and let the Security Council pass judgment on it. The P5 plus Germany have worked together over the past three years, slapping a series of UN resolutions and sanctions on the regime in Iran for defiance over its suspect nuclear work, yet Russia and China have doggedly watered down each text, line by line.

Doing it for themselves

There is much the UN Security Council will never be able to do, no matter who occupies its plushest seats. And there are lots of other ways to get useful things done these days. The internet helps campaigners on human rights, as on other issues, to get their message round the world rather effectively. Stung by constant exposure and criticism of its policy in Sudan and Darfur, China appointed a special envoy (who soon found he had a lot of explaining to do) and shifted ground on the need for a UN

force, even though deployment is agonisingly slow.



In some cases, regional organisations are better equipped to take the strain. Enlargement of the EU and NATO has helped stabilise Europe's borderlands, with mostly European troops and police these days in the Balkans. Russia may protest, but its western frontier has never been more peaceful.

On a similar principle of African solutions to African problems, the African Union has provided troops in Sudan and elsewhere. But devolving security jobs to the neighbours can be a disaster: the AU delegated the problem of what to do about Zimbabwe's Robert Mugabe to a southern African grouping, SADC, which left it to South Africa's Thabo Mbeki, who did nothing. The hard-pressed people of Zimbabwe are still waiting for relief.

East Asia, the other big potential battlefront in the cold war, used to look very different from Europe, which has long had more than its share of shock-absorbing regional clubs and institutions. Now, alongside the Association of South-East Asian Nations (ASEAN), a still limited talking-shop, other regional conversations are starting up. The ASEAN Regional Forum draws in not only China, Japan and Korea, but Americans, Russians and Europeans; ASEAN-plus-three summits are clubbier, involving only regional rivals China, Japan and Korea. A new East Asian Summit excludes America but brings in India and Australia, among others; Americans naturally prefer to boost the Asia-Pacific Economic Co-operation forum (APEC). Meanwhile Russia, China and their Central Asian neighbours have founded the Shanghai Co-operation Organisation, in part to counter Western influence in the region as NATO battles on in Afghanistan, but in part so that Russia and China can keep an eye on each other. Annual joint military exercises are a new feature.

Problem-solving groups come in all shapes and sizes, from quartets (for promoting Middle East peace or trying to settle the future of Kosovo) to entire posses. Some 80 countries in the Proliferation Security Initiative (an "activity not an organisation") exchange information and train together to sharpen skills for blocking illicit shipments of nuclear or other weapons materials. Like the P5 plus 1 talks on Iran (sometimes called the E3 plus 3 by Europeans), there are six-party talks hosted by China on North Korea (and including America, South Korea, Japan and Russia), which could yet evolve into a formal north-east Asian security dialogue.

More countries are taking the initiative. China, Japan and South Korea, East Asia's rival powers, will meet this year for a first 3-minus-ASEAN summit. China, India and Russia meet from time to time to re-swear allegiance to multipolarity. They may have little more in common than an ambition to put Europe and America in the shade, but earlier this year the foreign ministers of the four BRIC countries got together for the first time; their economic and finance ministers will soon meet too. And with a wary eye to China's growing economic and military weight, America, Australia and Japan have formed something of a security threesome, though Japan's plan to include India too was deemed a bit provocative.

Quirky but familiar globe-spanning organisations include the Commonwealth, which knits together Britain's former colonies plus other volunteers and does good works in all sorts of out-of-the-way places, and the Non-Aligned Movement, a cold-war hold-over with 116 members and communiqués that leave no prejudice unrecorded. But what of Mr McCain's endorsement of a League of Democracies?

The notion isn't new. An American sponsored Community of Democracies got going with fanfare in 2000. There is nothing wrong with mobilising freedom-loving governments to speak up for democracy. But there are difficulties.

Last time, America found it hard to say no to friends, and not all its friends are democrats. The new League (or Concert) of Democracies would have clearer rules for ins and outs. Supporters see it as potentially an alternative source of legitimacy, should the Security Council be hopelessly divided: a two-thirds majority of

the roughly 60 countries that might qualify could even authorise the use of force to deal with threats to peace or to uphold the principle of a "responsibility to protect".



But would a group of countries that spans all continents from Botswana to Chile, and Israel to the Philippines, ever manage to agree on much? A supposed democracy caucus at the UN has achieved little. Dividing the world ideologically again seems a step backwards to some. Nor could such a club solve pressing global problems. Coping with climate change needs China as well as India; energy security needs Saudi Arabia and Russia, as well as oil-dependent Japan or the Europeans.

The good news, given the rise of lots of new powers and players, is that this is not the 19th century. Then governments had few means other than gunboats to settle their differences. There are plenty of guns about these days, but also many other ways to settle the world's disputes.

The presidential election

White men can vote

Jul 3rd 2008 | WARREN, OHIO
From The Economist print edition

And there are a lot of them, even if they can't dance

AP



IN A family restaurant with bottomless coffee, Paul Radaker chews on a battered fish. A retired carpenter, he has been a Democrat all his life. But this year, he is leaning towards John McCain. The Republican candidate is a war hero, he observes. Barack Obama may be intelligent, but "I don't really know what he stands for."

Mr Obama's race "doesn't bother me at all", says Mr Radaker. The question sparks an anecdote about the Korean war. The southern guys Mr Radaker met when he served there "really didn't like blacks," he recalls, "But I guess that's changed now." Still, he reckons that plenty of people round here will not vote for Mr Obama because of his colour.

Mr Radaker is white and 78. A few miles away, John McCain is taking questions from workers in a car factory, who are mostly white men too, but much younger. The car industry in the rustbelt is miserable. Factories making thirsty pickup trucks are cutting back or closing. But the General Motors plant at Lordstown is doing just fine. It makes a small car, the Chevy Cobalt, which sips petrol in moderation and is therefore selling well. Mr McCain is touting this, along with GM's plans for a plug-in hybrid car, as evidence that American ingenuity can solve a lot of problems, from high petrol prices to global warming. He has trouble remembering the names of the cars he has just seen being made, but he thinks they look great.

The workers are polite, but hardly ecstatic. Many are socially conservative, but pocketbook issues trouble them more. "I'm undecided," says Matt Cope, a 34-year-old assembler who hunts and prays like a Republican but thinks the Democrats are more focused on workers. "John McCain has suffered a lot [he was tortured by the North Vietnamese]. He's a good man. But Obama's a stand-up guy, too."

Guys like Mr Cope could decide the election. According to the polls, Mr Obama beats Mr McCain in nearly every group except white men. Unfortunately for Mr Obama, there are a lot of white men. In 2004 they were roughly 36% of the electorate, and they preferred George Bush to John Kerry by about 25 points. This year, Mr McCain leads Mr Obama by about 20 points among them.

Democrats have various theories about why white men do not like them. One is that the problem is only with southerners, who abandoned the Democrats in the 1960s because President Lyndon Johnson signed

laws demanding equal rights for blacks. Clearly, there is some truth to this. But it is not the whole story. For one thing, the Democrats lost many non-southern white men, too. Between the presidential elections of 1960 and 2004, their share of the southern white male vote shrank by 17 points, but among non-southern whites it still shrank by 12 points. And racial attitudes have changed dramatically since the 1960s, especially among the young. There must be something besides bigotry making white men spurn the Democrats.

Thomas Frank, the author of “What’s the Matter with Kansas?”, thinks the white working class has been hoodwinked. It is in their economic interest to vote Democratic, but they don’t because those crafty Republicans have got them all worked up about silly moral and cultural issues such as abortion, guns and gay marriage.

Both theories are popular among Democrats, not least because they imply that Democrats have done nothing wrong; it is just that poor white trash are too bigoted or stupid to support them. But Democrats will not get very far by blaming the voter. David Paul Kuhn, author of “The Neglected Voter: White Men and the Democratic Dilemma” points out that moral issues cannot easily be separated from economic ones. Poor people fret more about family breakdown because they see more of it than rich people do and its consequences, for them, are worse.

In a time of economic insecurity, it is rational for people to turn to things they can rely on, such as faith and patriotism, and unwise for Democrats to scorn them for it. That is why Mr Obama’s comment that people in small towns “cling to guns or religion or antipathy to people who aren’t like them” because they are “bitter” will be the keystone of Republican attacks, predicts Mr Kuhn.

Mr Kuhn thinks the Democrats’ failure to take white men seriously is the main reason they keep losing presidential elections. The party captures liberal white men—typically prosperous professionals—but scores badly among businessmen and white male workers. Part of the problem is that Democrats are identified with the notion that white men are to blame for all the world’s ills, from racism to the oppression of the workers. Few white men share this view. Many are workers themselves.

The Republicans have long been better at presenting themselves as the Daddy party, self-reliant, tough on crime and tough on terrorists. “They talk male talk,” grumbled the late Norman Mailer, a novelist who thought liberals could be macho too. The Democrats, meanwhile, strike some white men as effete, cosmopolitan and condescending. Mr Obama’s waffly explanation as to why he temporarily stopped wearing a flag pin sounded awfully as though he thought those who love the flag are frauds and dolts.

In some voters’ minds, Democrats are associated with an assault on masculinity itself. “Boys can’t be boys in school any more,” complains Karen Combs, a volunteer for Mr McCain. And urban liberals don’t understand how much guns matter to rural white men, fumes Dave “Mudcat” Saunders, a Democratic strategist. “Someone’s talking about taking your guns, they’re talking about coming inside your fence,” he says. “And government should stop at your fence.”

If the Democrats paid more attention to “Bubba” (the white male rural voter), they could get a lock on the presidency for 30 years, predicts Mr Saunders, with the hyperbole common to his trade. The first step is showing up: “If you live in Kentucky or West Virginia and you read in the local paper about a candidate who isn’t coming ’cause he thinks you won’t vote for him, you won’t vote for him.”

Mr Obama seems to understand this, and is striving manfully to make it up to Bubba. He has reversed his old view that the gun ban in Washington, DC, (which the Supreme Court struck down last week) was constitutional. He stresses that big cities and rural areas can have different gun laws, saying that “what works in Chicago may not work in Cheyenne”. He gave a rousing speech about patriotism on June 30th, including an anecdote about sitting on his grandfather’s shoulders watching American astronauts come to shore in Hawaii. And the next day, he gave a speech in Ohio about faith.

But he has his work cut out. The “people” section on his website divides Americans into 17 categories: Latinos, women, First Americans, environmentalists, lesbian, gay, bisexual and transgendered people, Americans with disabilities, Asian-Americans and Pacific islanders and so on. There is no mention of whites, or men.

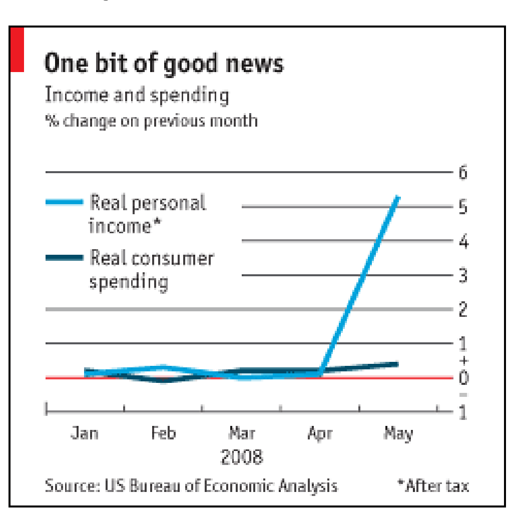


Economic policy

What next?

Jul 3rd 2008 | WASHINGTON, DC
From The Economist print edition

Congress ponders how to throw more money at the slumping economy



FOR months Washington has waited for the economic stimulus plan George Bush signed in February to take effect. And now it has, earlier than some expected. The government reported on June 27th that the tax rebates included in the package helped increase real after-tax incomes by 5.3% in May, and consumers increased their spending at twice the rate they did in April.

Still, as even George Bush admitted at the time of announcing it, the stimulus will be no more than a temporary "booster shot". Stimulus or no, the government announced on July 3rd that employers cut another 62,000 jobs in June. That is the sixth straight month of job losses. And despite the stimulus's help raising incomes in May, wages still lagged behind inflation, reflecting the weak labour market and rocketing prices for commodities, especially oil. Consumer confidence is now lower than in the last three recessions. House prices continue to fall, and Wall Street worries about more huge losses at big banks. All ominous enough to get policymakers talking seriously.

Congress is therefore pondering what to do next. This month it is likely to pass a long-debated housing bill, which would allow some at-risk borrowers to refinance into government-backed mortgages. The Congressional Budget Office estimates that some 400,000 borrowers will be able to take advantage of the scheme; the bill's backers insist the number could be as high as 1.5m. Still, with perhaps 3m foreclosures expected this year, nobody thinks the measure will solve the housing market's problems. Barney Frank, one of the bill's authors and the chairman of the House financial services committee, has said a second housing bill may be in order.

But Nancy Pelosi, the House's speaker, wants a second stimulus package before any new housing legislation. Indeed, some prominent economists are now arguing that, in the words of Robert Shiller of Yale, policymakers should be designing a new stimulus plan and should "stand ready for another after that, and another".

Details are still emerging. But Democrats are keen on helping state governments—which in the first quarter saw their lowest annual growth in tax revenue since 2002—by increasing money for Medicaid, the health programme for the poor that the states fund jointly with the federal government. That could prevent states from having to cut benefits in order to balance their budgets. Barack Obama has spoken of more rebate cheques. Others suggest a holiday from the payroll tax. The Democrats say they want to spend another $50 billion on the whole package. But it could be triple that if the outlook worsens.

Getting a second stimulus plan or more debt reduction for homeowners past the White House could be difficult. George Bush is wary of the housing bill, worrying that it rewards irresponsible borrowers. Congressional Republicans might support rebate cheques, but would probably oppose plans for more social spending.

Much depends on how the economy fares in the coming weeks. Nothing focuses politicians' minds like an economic slowdown in an election year. If the president vetoes any of these bills, a nervous Congress might override him.

Gun control

Showdown

Jul 3rd 2008 | AUSTIN AND TAMPA
From The Economist print edition

Gun owners are becoming emboldened. That may be premature

AP



Are you looking at me?

ON JUNE 26th the Supreme Court overturned the District of Columbia's handgun ban and asserted that individuals have the right to own guns. Gun enthusiasts rejoiced. But as they move to capitalise on this favourable judgment, they may run into new problems.

Consider two developing gun-rights controversies. On July 1st Florida became the fourth state to allow people to bring their guns to work. The gun has to stay locked in the car, and its owner must have a concealed-weapons permit. You cannot bring your gun if you work in a school, hospital, prison or power plant.

The law is good news for Floridians with a dangerous commute. Those who like to go hunting after work are also excited. But the prospect of heavily fortified strip-malls alarms others. The state leads the nation in concealed weapons permits; half a million people have them.

Florida Democrats opposed the measure. But its passage has a silver lining for them. The law has created a rift between two old allies in the Republican Party: the gun-rights crowd and business owners. The latter believe that it conflicts with their property rights. Employers are not allowed to ask workers if they have a gun in the glove box. If an employee opens fire at work, worries Irwin Stotzky of the University of Miami, the employer could be held responsible in a civil suit. The Florida Chamber of Commerce and the Florida Retail Federation are suing to overturn the law. Robert Hinkle, a Tallahassee judge, will weigh in later this month. He has already said that the law is poorly written and "stupid". Guns at work could be a useful election-year issue for Democrats.

A similar development is brewing in Texas. The state welcomed the Supreme Court's decision. Its senior senator, Kay Bailey Hutchison, was a leading opponent of the District's gun ban. She herself keeps "the normal handguns and shotguns" at home. But now there is a controversial movement afoot to allow people to carry their handguns openly, as the cowboys used to do. Texas is one of only six states where guns must be hidden. "Open-carry" advocates say that carrying a gun is natural, and that having to hide it is unfair. They add that people wear lots of things on their belts, such as BlackBerrys. Almost 18,000 people have signed one online petition. One supporter recently had two chainsaws stolen in a parking lot, and he said it would never have happened had he had his gun handy.

In this case, too, most Democrats are appalled. But they can let Republicans take up the fight for them. Plenty of gun proponents oppose open-carry. Joe Driver, a Republican representative from Garland, is more interested in efforts to get Texas its own guns-at-work law. As for the open-carry movement, he likes the idea that criminals don't know who is carrying a gun. That way, perhaps, they have to be extra careful.

The death of yearbooks

Valete

Jul 3rd 2008 | ST LOUIS
From The Economist print edition

A tradition in decline

ONE fixture of college life is rapidly disappearing. Yearbooks, those beloved annual publications recording the events and people of the academic year, are suffering from plummeting print-runs, or are even being dropped altogether, in colleges across the country.

The phenomenon is due in part to the price of the hard-bound volumes, typically as high as $75. For cash-strapped students facing ever-rising tuition and living costs they are a luxury that many can't afford. But the main cause is not the cost so much as the replacement of print with electronic media by and for the Facebook and MySpace generation. With social networks linking hundreds of friends and offering digital photographs and videos the traditional yearbook looks like a bit of a dinosaur.

After more than a hundred years of publication Purdue University, in Indiana, has published its last yearbook, as has nearby DePauw University. Even where colleges have tried to adapt to the new media by, for instance, including DVDs summing up the year along with the print version, yearbooks are attracting few students, readers or editors.

McKendree University is the oldest college in Illinois. Inside its historic buildings, some dating back to the 1820s, its 1,500 students use the latest technology. Although the university still publishes a yearbook, the print-run is a mere 150 copies, only half of which are bought by students. Being on the staff of the yearbook used to be considered prestigious: now only eight students show up for the job. The downturn in print publications has also hit magazines for alumni. These, for instance at McKendree, are increasingly being replaced by online editions.

Yearbooks are hanging on in American high schools but the future is unclear. Parents and students complain about the high prices, and a generation that has never known a time before the internet is losing interest.

Although today's students find yearbooks old-fashioned, they may one day miss their vanished youth. Long after Facebook and MySpace have become obsolete and the electrons dispersed to the ether, future alumni might just wish for the permanence of ink on paper.

The Green Congress

Could do better

Jul 3rd 2008 | WASHINGTON, DC
From The Economist print edition

Democrats in the House and the Senate have not been as green as their word

WANDER through the marble hallways of Washington’s Capitol and look up. Screwed into the sconces and lanterns of one of the city’s oldest buildings are the glowing helices of very 21st-century compact fluorescent bulbs. Downstairs, Hill staffers eat off compostable plates. And soon the spotlights that illuminate the Capitol’s great dome—so inefficient that their heat requires workmen to wear special suits in order to handle them—will be replaced with more efficient LED bulbs.

Nancy Pelosi, the speaker, came into office last year promising a slew of green initiatives, including an overhaul of her House of Representatives itself, which is on track to be carbon-neutral by December. More significant are the legislative achievements the Democratic majority proudly touts, particularly last year’s passage of the first increase in car fuel-efficiency standards for three decades. Now Congress is moving to preserve millions of acres of wilderness, far more than it has done in preceding years, setting aside land in states from California to West Virginia.

But this Congress’s record is still far from impeccable. Along with the new efficiency standards, it approved a generous sop to America’s ethanol industry in the shape of a sharp increase in the amount of home-grown ethanol that has to be added to America’s fuel. Environmentalists say that ethanol from maize takes too much energy and water to produce, and they worry that farmers are bringing acres out of conservation programmes and into cultivation to satisfy the requirement. The run-off attributable to ethanol production, a recent paper in the *Proceedings of the National Academy of Sciences* estimates, could increase the size of the Gulf of Mexico’s “dead zone” by a fifth by 2022.

Congress’s recent farm bill was supposed to dull the incentives for American farmers to plant on marginal lands by slashing farm subsidies and beefing up conservation programmes. But the Democrats sweetened the subsidies instead. Coal-state senators have even thwarted Ms Pelosi’s green Capitol effort by insisting that the fume-spewing plant that heats and cools the building—one of the dirtiest facilities in the city—continue burning the fossil fuel.

Perhaps the record would be better if Republican senators hadn’t recently killed off a bill to establish a cap-and-trade regime for carbon emissions? True: but the policy was poorly designed. It limited Americans to buying carbon offsets only from foreign outfits that do not directly compete with American ones, which would have made the system very inefficient, and it unreasonably threatened tariffs on nations not doing enough to curb carbon emissions by 2014.

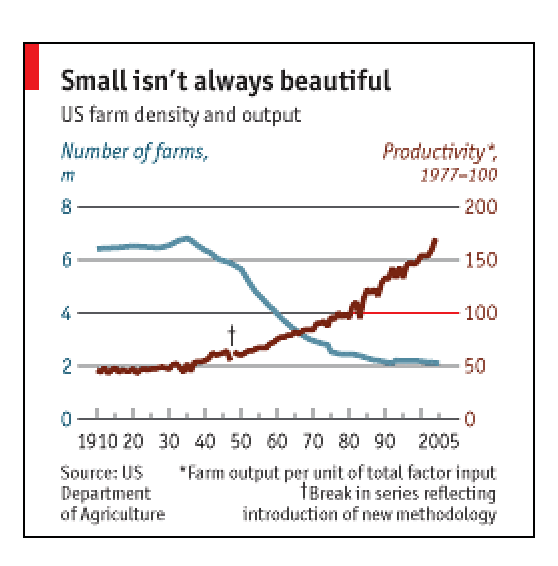
For now, environmentalists recognise that the Democrats’ majority is slender and reliant on conservative, farm-state lawmakers. They will expect much more in coming years. Whether John McCain or Barack Obama is the next president, he will be more attentive to green issues: and everyone expects larger Democratic majorities in Congress. If the Democrats’ coalition fails to satisfy America’s greens under those conditions, their patience will surely start to dim long before Ms Pelosi’s new light bulbs do.

Farming

Needles in a haystack

Jul 3rd 2008 | MEAD AND RANDOLPH
From The Economist print edition

Small family farmers in the new era of agriculture



CORN blankets eastern Nebraska in the summer. Straight roads glide over the hills, dividing the fields like measuring tape—in the 19th century the Homestead Act sectioned the land into neat plots for new settlers. Patty Coady's family did not get their farm from the act, but they are hardly newcomers. They bought their land more than 100 years ago.

In some ways little has changed. Ms Coady and her brother farm 280 acres (113 hectares), and have some cattle, sheep and goats. But this is a booming new era. Prices for commodities and land have shot up. The new farm bill is fat with subsidies. Farmers' average income is projected to rise to $89,434 in 2008, up 6.3% over last year. Most of the bonanza, though, is being scooped up by the big operators. Ms Coady sighs, leaning against a giant tractor tire. "Small farmers can hardly compete."

Family farms are hardly a fraught minority—97% of America's farms were family-owned in 2006, the most recent year for which figures are available. But not all family farms are created equal. In 2006 "big" family farms (defined as those with sales above $250,000 a year) comprised 7.6% of the total number, but accounted for 61% of production. While big family-farmers earned 68% of their income simply from farming, small farmers had to earn most of their money elsewhere. Some 63% of all farms were owned either by retirees or by those whose main job was not farming. Ms Coady falls in the 27% who were small farmers describing farming as their main occupation. But even this group earned most income from other sources, like side jobs and dividends.

The decline of small farms is well documented. Since the 1930s agricultural innovation and a rise in non-farm employment have driven productivity up and the number of farms down. Nebraska had 135,000 farms in 1934; last year it had about 47,300.

The government's role in this progression is up for debate. "Change is inevitable," says Mike Korth, a farmer in north-east Nebraska, "but I don't agree that the government should have a heavy hand in determining that change." Though Mr Korth receives commodity payments from the government, he has become an avid critic, travelling to Washington with Nebraska's Centre for Rural Affairs (CFRA), an advocacy group. Subsidies, Mr Korth and his allies say, help big farmers to bid up land prices and make it harder for small farmers to survive.

Rather than accelerate change, Mr Korth and the CFRA wish the government would help to stem it. Chuck Hassebrook of the CFRA argues that small farms sustain the rural middle class; consolidation drains it. But government can hardly stop farms from evolving. The CFRA this year supported legislation in Nebraska to limit corporate farming, but the bill failed.

More successful, or at least more sustainable, have been government efforts to boost young farmers. In 2004 about 27% of farm operators were 65 or older, compared with 17% in 1969. High entry costs, such as land and equipment, keep many younger farmers away. More than 20 states have programmes to attract them, according to the Council of State Governments (CSG), a non-partisan policy group. Nebraska has tax credits for landowners who rent to young farmers. The new farm bill also offers help through loans and grants—one programme would prioritise loans for beginners who practise organic farming.

Such niches, says Carolyn Orr of CSG, may help small farmers survive. But consolidation is likely to

continue under the next generation of farmers. “If they want to make farming a full-time job,” she asks, “what other option do they have?”

Lexington

Michelle Obama's America

Jul 3rd 2008
From The Economist print edition

Is Barack Obama's wife his rock or his bitter half?

Illustration by Kevin Kallaugher



THERE are two ways to be a political spouse. You can shun the limelight or you can grab it. Margaret Thatcher's late husband, Denis, exemplified the former approach. He never upstaged his wife and though intelligent and rich, he was content to be viewed as a golfing, gin-swilling duffer. At the opposite end of the spectrum are the Clintons. Hillary was Bill's closest adviser when he was president, and he would have done the same for her, had she been elected. Neither approach is right or wrong, but both have predictable consequences. If you keep your mouth shut, you are unlikely to stir up controversy. If you speak up, you may help your spouse, but you risk hurting him or her, too.

John McCain's wife, Cindy, gazes adoringly at him on the stump but says little. If she has to introduce him, she says she loves him and hopes you will vote for him. She may favour pink skirt-suits over golfing trousers, but in her reluctance to say anything that might conceivably hurt her spouse she is unmistakably a (Denis) Thatcherite. Hostile bloggers half-heartedly accuse her of being a Stepford wife or make snide cracks about the fortune she inherited and her past addiction to painkillers. But she seldom captures the headlines and seems to like it that way.

Michelle Obama falls somewhere between the two poles. Unlike Bill or Hillary, she has never hinted that she expects to be co-president. But unlike Mrs McCain, she criss-crosses the country making fiery speeches on her husband's behalf. In many ways, she is a huge asset to his campaign. She is clever, driven, beautiful and articulate. Even when he is not there, she draws large, avid crowds. Yet she still finds time to be supermum. She bought two laptops so her husband can see and talk to his daughters when he is on the road. She teases him about his snoring and makes him take out the rubbish. He calls her "my rock".

Like her husband, she exemplifies the American dream, having risen from humble roots to Princeton, Harvard and a $275,000-a-year job handling "community and external affairs" and "business diversity" for a hospital in Chicago. But her story is otherwise quite different from his. His background is more exotic and chaotic. His mother was white, his father was Kenyan, they broke up when he was two and the young Barack later lived in Hawaii and Indonesia. Michelle's family, by contrast, was hard-up but intact. It was also all-black, all-American and rooted in the South Side of Chicago. Michelle grew up knowing useful people: she was chummy with Jesse Jackson's daughter and even baby-sat his son when she was a teenager.

When Barack was starting out as a politician, his rivals dismissed him as inauthentically African-American or even “the white man in blackface”. Having Michelle at his side helped reassure sceptical blacks that he was really one of them. Even the precise shade of her skin colour may have helped him at the polls. Famous black men often pick light-skinned or white wives. Some black women resent this. That Michelle is quite dark may have endeared Barack to black female voters who might otherwise have voted for Hillary Clinton.

Now that the primaries are over, the issues have changed. Blacks are solidly for Mr Obama, but many swing voters are unsure. Some Republicans think his wife’s habit of speaking her mind could prove a problem. For example, in February, as her husband’s campaign was catching fire, she said: “For the first time in my adult life, I am proud of my country, because it feels like hope is finally making a comeback.” Some Americans bristle at the implication that the only worthwhile thing any of them has done in the past quarter-century is to back Mr Obama.

Mrs Obama’s speeches rarely accentuate the positive. America, to her, is a “downright mean” country where families struggle to buy food, where mothers are terrified of being fired if they get pregnant and where “life for regular folks has gotten worse over the course of my lifetime”. But she was born in 1964, when Americans lived shorter, poorer lives and southern blacks couldn’t vote. Whereas her husband is magically skilled at not giving offence, Mrs Obama can be a blunt instrument. “Don’t go into corporate America,” she urges young people, denigrating what most Americans do for a living and biting the hand that pays for all the public programmes she favours. “Barack Obama will require you to work,” she says. “He is going to demand that you shed your cynicism. That you put down your divisions. That you come out of your isolation…Barack will never allow you to go back to your lives as usual, uninvolved, uninformed.” Some people would rather decide for themselves how to live their lives.

The bitter bit

Conservative pundits have savaged her. One acerbic blogger calls her “Obama’s bitter half”. Others mock her occasional gripes about her personal finances and her solipsistic college thesis about the woes of black Princetonians. The *National Review* says she “embodies a peculiar mix of privilege and victimology, which is not where most Americans live. On the other hand, it does make her a terrific Oprah guest.”

Mr Obama says people should lay off his wife. Laura Bush agrees. And one has to sympathise with Mrs Obama. She was always a reluctant political wife. Her husband’s crazy hours and long absences impose a hefty burden on her and on their children. In dark moments, she fears for his physical safety. And all the while, both she and her husband are subjected to maliciously false gossip online.

But not all criticism is unfair. If Mr Obama is president, his wife will have the ear of the most powerful man on earth. So her political views matter. And if she expresses them forcefully in speech after speech, she can hardly cry foul when not everyone likes what she says. On June 30th she appeared on the front page of *USA Today* saying: “I don’t want to be a distraction.” For better or for worse, she is.

Colombia

Uribe's hostage triumph

Jul 3rd 2008 | BOGOTÁ
From The Economist print edition

The freeing of Ingrid Betancourt (left) and other guerrilla hostages is a political apotheosis for President Álvaro Uribe (right). It might even secure him a third term

AFP



IT WAS an ending happier than any Hollywood director would dare to dream up. After years of captivity at the hands of left-wing FARC guerrillas, Ingrid Betancourt, three American defence contractors and 11 Colombian soldiers were rescued on July 2nd by the army without a shot being fired. It was a “miracle”, said Ms Betancourt, a former presidential candidate who holds French and Colombian nationality and who had been held for more than six years, for much of that time in chains and in poor health. It was a triumph for Colombia’s president, Álvaro Uribe, who at some political cost had resisted pressure to negotiate the release of Ms Betancourt. And it was a disaster for the FARC and its sympathisers in Latin America who hoped to use the hostage issue to weaken Mr Uribe.

The rescue operation involved years of planning. It was testament to the army’s new sophistication in intelligence and infiltration. It built on its recent successes in disrupting the FARC’s communications and isolating its leaders from each other. An attempt to rescue other guerrilla hostages in 2003 had ended in disaster, when ten were killed by their captors.

This time the army relied on trickery rather than surprise or force. A former hostage who escaped last year supplied details of the jungle camps where the hostages were being held in the remote south-eastern departments of Guaviare and Vaupés. Army intelligence agents, posing as senior FARC members, communicated with the guerrilla commander guarding the hostages. They gave him a false order purporting to be from the FARC’s new leader, Alfonso Cano, that the hostages were to be taken to a helicopter sent by a humanitarian organisation—mimicking the arrangements when six other captives were released earlier this year after mediation by Venezuela’s president, Hugo Chávez.

Once on board the helicopter, the two guerrilla escorts were overpowered and the army agents, some dressed in Che Guevara T-shirts, broke the news to the hostages that they were flying to an army base and freedom. “We couldn’t believe it. The helicopter nearly fell because we jumped for joy,” said Ms Betancourt.

The operation is the latest of several devastating blows suffered this year by the FARC, which mixes an antiquated Marxism-Leninism with drug-trafficking and racketeering. In March, the army bombed a guerrilla camp just over the border in Ecuador, killing Raúl Reyes, a member of the group’s seven-man secretariat. The incident outraged Ecuador’s president, but yielded a huge haul of documents from Mr Reyes’s computers. Days later another member of the secretariat was killed by his own bodyguard. Then

Manuel Marulanda, the FARC's founder and undisputed leader, died, supposedly of a heart attack.

The FARC still hold several hundred hostages, including a score of army and police officers and two politicians. But they have lost their chief prizes. Ms Betancourt was a minor politician in Colombia when she was seized while campaigning for the presidency in 2002. But she has become a national *cause célèbre* in France, where she studied; she married a Frenchman and her two children live there. Nicolas Sarkozy, France's president, had made her release a personal priority, and pressed Mr Uribe to negotiate with the guerrillas.

The three Americans, who were working on contract to the United States government, were captured when their anti-drug surveillance plane crashed in guerrilla territory in 2003. The United States supplies Colombia with military aid and training. It has given particular help in intercepting FARC communications. Juan Manuel Santos, the defence minister, said that he had co-ordinated the rescue plan with American officials.

The FARC claimed to want to swap its trophy hostages (who at one point numbered around 60, including Colombian politicians and military officers) for jailed guerrillas. But e-mails from Mr Reyes's computer, seen by *The Economist*, show that their real aim was to use them to embarrass Mr Uribe politically and to gain international recognition.

They wanted the president to "demilitarise" a swathe of territory to allow talks. Mr Uribe was resolutely against that: during past peace talks the FARC used a similar enclave for recruiting and training while continuing to kill and kidnap. The guerrillas also want the European Union to drop them from a list of terrorist organisations—an aim that Mr Chávez supported, calling for their recognition as a "belligerent force".

Mr Uribe faced much pressure to bow to the FARC's demands, both from the hostages' families and, less understandably, from France. (At Mr Sarkozy's request he freed a jailed guerrilla leader who has returned to action.) Ms Betancourt's mother was particularly bitter in her criticism of the president during her tireless campaign for her daughter's release. But Ingrid Betancourt was full of praise for Mr Uribe and for the "impeccable" army operation. She said the biggest blow suffered by the FARC had been when the president succeeded in changing the constitution to allow him to run for—and win by a landslide—a second term in 2006.

That statement must have been particularly sweet for Mr Uribe. For the hostage release came in a week in which he was being widely criticised at home for appearing to blow up a conflict with Colombia's judiciary in order to engineer the possibility of a third term. Enraged by a Supreme Court ruling on June 26th that seemed to question the legality of his election victory in 2006, he has proposed a referendum on rerunning the vote.

The court's verdict involved Yidis Medina, a former congresswoman who cast the deciding vote when a congressional committee approved the constitutional change that allowed Mr Uribe to run in 2006. Ms Medina, a disreputable character who is also being investigated for alleged links to the ELN, another guerrilla group, had given a videotaped interview in 2004 in which she said that three of her followers were given government jobs in exchange for her vote on the re-election amendment. She authorised the tape to be made public after other promises were not kept, she said.

The court sentenced Ms Medina to 47 months of house arrest, and ordered investigations into two ministers she claimed had been involved in arranging the jobs. It went on to ask the Constitutional Court to consider the legality of the amendment and thus of the 2006 election in which Mr Uribe won by a landslide.

In a late-night television address, the president blasted the Supreme Court for "abuse of power" and for "applying justice selectively". It is not the first time that Mr Uribe has clashed with the courts. Under Colombia's constitution, the Supreme Court has the power to investigate wrongdoing by members of Congress. It has done so with energy: most of the more than 70 legislators it is investigating for past links with right-wing paramilitary groups are members of parties that backed the president; they include his cousin, Mario Uribe. The justices insist that they are merely applying the law. The president has repeatedly questioned their impartiality.

Legal experts doubt the constitutionality of a referendum to call for a rerun of an election. Many political commentators say it is unnecessary, since the Supreme Court did not directly question the legitimacy of the election itself. Nevertheless, the government announced that it would present a referendum bill when

Congress begins a new session on July 20th. The referendum could not be held until late 2009. So a rerun of the 2006 election might be held just before the next scheduled presidential election in May 2010.

That timing makes Mr Uribe's opponents suspicious. For months he has refused to rule out seeking another constitutional change that would allow him to stand for a third term. His supporters are collecting signatures for a separate referendum on this issue. The triumphant release of the hostages, coming on top of his other successes, means that if he indeed wants a third term, Mr Uribe may well be able to get it. But others have political ambitions too. One is Mr Santos, who as defence minister has overseen those successes. Another is Ms Betancourt, who in freedom was quick to say she still aspires to the presidency. It would be even stranger than the movies if the three main protagonists in this week's happy ending were to meet again in a sequel at the ballot box in two years' time.



Canada

Green gambit

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From The Economist print edition

Stéphane Dion, the Liberal with a carbon-tax plan

Illustration by David Simonds



FANS of “Yes, Minister”, a 1980s British sitcom, will recall that whenever Sir Humphrey Appleby, the emollient civil servant, labelled a brainwave by his minister “courageous”, a climbdown was inevitable. That is the adjective being used by many of the supporters of Stéphane Dion, the leader of Canada’s opposition Liberal Party, to describe the plan for a national carbon tax that he unveiled with campaign-style fanfare in mid-June.

Despite a slightly wimpish image, Mr Dion, a former academic, certainly does not lack courage. On July 4th he was due to head for Alberta, Canada’s oil patch, to spend the weekend at the Calgary Stampede endeavouring to sell a tax expressly designed to curb energy use.

In theory, Mr Dion has hit on a winning issue. Latest figures show that Canada’s emissions of greenhouse gases are 30% above the current target set in the Kyoto protocol. Stephen Harper’s minority Conservative government lacks a serious plan to cut emissions. Many Canadians are embarrassed by this and care about the environment (see article).

But at the moment they are more worried about a slowing economy and rising energy costs. So they are unlikely to welcome higher fuel taxes, as Mr Dion proposes. He insists that his tax proposals would be revenue-neutral: the carbon levy would be offset by cutting income taxes and by extra handouts for the poor. Petrol would be untouched because it already carries a 10% federal excise tax.

But Mr Harper, whose political roots are in Alberta, clearly smells blood. He calls the carbon tax “insane” and predicts it will not only “screw the West”, where most Canadian oil and gas is produced, but also “screw everybody across the country”. The prime minister’s unusually forthright language “is probably a good summary of how it will go over”, says Roger Gibbins of Canada West Foundation, a Calgary-based think tank. Even before the details were out, the Conservatives released a series of crude but effective internet ads featuring a talking blob of oil that warns viewers this “tax trick” would “drive up the cost of everything”.

Nevertheless, Mr Dion may still be on to something. A surprising number of business groups and economists have come out in support, if not of the tax itself, then at least of stronger federal policies to cut emissions. Federal passivity has led to some provincial governments taking their own initiative: British Columbia imposed its own carbon tax on July 1st, and Quebec did something similar last year. Even Alberta has a limited programme to trade emissions permits within the province. Ontario is leaning towards a cap-and-trade system, as is the federal government.

Business wants to see an end to this “policy chaos”, says Thomas D’Aquino, who speaks for Canada’s largest companies. It has not gone unnoticed that big trading partners, including the United States, have either put a price on carbon or are about to do so. Exporters worry that their products could be penalised if Canada does not follow suit.

Whether or not western Canada warms to his carbon tax, Mr Dion may derive some political benefit. Since becoming Liberal leader 19 months ago, he has been derided as ineffectual. But he is at his most confident when acting the policy wonk. His much-mocked English has improved.

Strengthening the Liberals’ green credentials might win the party new support at the expense of the

leftish New Democratic Party or the Green Party, a newish outfit which commands a steady 10% in the opinion polls although it has yet to win a seat in parliament. With the Liberals and Conservatives neck-and-neck in opinion polls, Mr Dion’s gamble that Canadians’ green instincts will trump their reliance on cheap energy might just decide who forms the next government.

Jamaica

Sick transit

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The murder of an anti-corruption campaigner

A PROMISE to root out corruption was one reason why Bruce Golding led his Jamaica Labour Party to an election victory last year, ending 18 years of rule by the People's National Party. But suddenly the battle to clean up government has turned bloody. On June 27th two gunmen murdered Douggie Chambers, the chairman of the Jamaica Urban Transit Company. He had gone out into the street for a quick smoke before signing an agreement with union leaders. Even in a country with one of the world's highest murder rates, his killing on June 27th came as a shock.

Mr Chambers was an accountant and a specialist fraud investigator brought in by Mr Golding on a token salary to reform the transit company, which runs the capital's bus service. It was losing over $25m a year, because of petty scams and a padded staff, with almost ten workers for each functioning bus. Several managers were fired within weeks. On the day he died, Mr Chambers had finalised redundancy terms for 485 workers.

For all its everyday violence, contract killings of public figures are rare in Jamaica. The finger was quickly pointed at the Klansman gang, which runs protection rackets around the bus depot in Spanish Town, the district where Mr Chambers was shot. His murder is a big setback for Mr Golding and for Jamaica, whose anaemic economy and indebted government are saddled with several loss-making state enterprises. The public sector already found it hard to recruit capable and honest managers, and will now find it harder.

The government is trying to clean up the customs, a "hotbed of corruption" involving private companies and officials, according to the finance minister, Audley Shaw. It is also reforming the National Housing Trust, which provides cheap mortgages. Last month it signed an agreement that turns the loss-making state-owned sugar industry into a joint venture with a Brazilian ethanol company.

Will Mr Chambers have died in vain? The government has sent a bill to parliament to appoint a special prosecutor to investigate corruption. A junior minister from the former government was charged in February with fraudulently extracting cash from a Cuban scheme which supplied free energy-saving light bulbs to Jamaican households.

Not everyone has been applauding the new government's efforts. The main business lobby complained that Mr Shaw's drive for tax compliance was "anti-private sector". After Mr Chamber's murder, it offered a reward of less than $7,000 for information about the crime. That will do little to ensure that his killers—and their associates—are swiftly caught and punished.

Canada's forests

Beetle attack

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From The Economist print edition

Pining for a cold winter



OVER the past 14 years, a tiny insect no bigger than a grain of rice has laid waste a swathe of British Columbia's forests so vast that the rust-red wasteland is visible from space. The mountain pine beetle has infested and killed over half the lodgepole pine forest in the centre of the province—an area larger than England. It has rampaged eastwards into northern Alberta for the first time. (It has also made localised attacks on forests in all 11 western American states.) Scientists now fear the voracious beetle is about to invade the jack pines of the boreal forest, which could see the plague sweep across northern Canada to the Atlantic coast. It is an unprecedented infestation that could become a catastrophe.

The pine beetle is a well-known pest, not an exotic import, but no effective means has been found to stop it. The beetles swarm up trees in large numbers, killing them by boring through the bark, sapping their nutrients and emitting a damaging blue fungus. Cold winters and forest fires normally keep the beetle populations in check. Some forest scientists trace the current outbreak to 1994, when provincial-government foresters, fearing the ire of greens, failed to eradicate a small infestation in a provincial park by cutting and burning. In any event, recent British Columbian winters have not been cold enough to kill the beetles.

The infestation is gathering pace: foresters fear that by 2013 four-fifths of British Columbia's central-southern pine forest will be gone. Wafted eastwards by strong winds, in 2002 the beastie made its debut in northern Alberta and further south in the national parks of Jasper, Banff and Kananaskis on the eastern slopes of the Rocky Mountains. It has advanced 400 kilometres (250 miles) across the province to Slave Lake. The beetle is now established in Alberta, despite vigorous cutting and burning.

It is closing in on the vast boreal forest. It is only 100km from the nearest outbreak, and winds can carry newly-hatched pine beetles up to 300km a year, notes Allan Carroll of the Canadian Forest Service. The boreal forest is mainly composed of jack pines, which lack the natural defences of the lodgepole pine; this has evolved in coexistence with the beetles.

The hope is that the infestation will stall on Alberta's eastern border with Saskatchewan, where large stands of jack pine are scarce. Better still would be a long, bitterly cold winter like those that were common until the 1980s. "Climate change is unequivocally affecting the outbreak," says Mr Carroll. They may be big energy consumers, but many western Canadians have also started to worry about what carbon emissions may be doing to their beloved forest.




Sri Lanka

The war president

Jul 3rd 2008 | COLOMBO AND TRINCOMALEE
From The Economist print edition

Reuters



Sri Lanka's army chief says the government has won its 25-year war against the Tamil Tigers. This is not true

Get article background

MAHINDA RAJAPAKSE, Sri Lanka's president, shakes out his white outfit and spreads his bare toes with a satisfied air. "We have concentrated on the LTTE [the Liberation Tigers of Tamil Eelam]," he says, "because unless we defeat them, we will have no peace and development." In January he abrogated a ceasefire and stepped up a brutal two-year offensive against the no-less-brutal LTTE. This week his army commander, General Sarath Fonseka, claimed the operation had succeeded. The Tigers, said the general, had lost the capability of fighting as a conventional army. "We have defeated them."

The Tigers have not surrendered and would presumably disagree. But the president's brother, Gotabhaya Rajapakse, who is also defence secretary, says the government has a once-in-a-generation chance to crush them. General Fonseka claims the Tigers have lost 9,000 fighters since 2006. They were driven from one big Tamil town, Jaffna, in 1995. Now they no longer pose a threat to another, Trincomalee.

In 2005 they enforced a boycott of a presidential election in the areas they controlled. Last year they were driven from the eastern part of their northern stronghold and failed to stop the ensuing provincial vote (one that most independent observers considered deeply flawed). The Tigers split in 2004. One of the group's former child soldiers, Sivanesathurai Chandrakanthan (known as Pillayan), whose still-armed militia contested the election as born-again democrats, has become chief minister of the Eastern Province—the highest-ranking elected office held by a Tamil.

Perhaps most important, the LTTE is said to have lost much of its foreign backing. Two years ago Tamil organisations could still raise money freely in Europe. Now, the LTTE are on many terrorist lists (America's Federal Bureau of Investigation dubs them "the most dangerous and deadly extremists in the world"). Canada has added the World Tamil Movement, a Tiger front, to its banned list; Italy has arrested 33 suspected LTTE financiers in one of the biggest crackdowns in years.

Yet it is much too soon to declare victory. The Tigers, a small guerrilla force of around 5,000 fighters, have repeatedly resisted conventional attack. In the 1980s, they beat back India's army. Their fearsome leader, Velupillai Prabhakaran, remains at large. Trincomalee bristles with soldiers and checkpoints. Even if they were to lose the territory they hold, the Tigers could still sink back into the local population and launch attacks from there.

For that reason, says President Rajapakse, the real test of whether the Tigers are defeated will be their willingness to lay down their arms and negotiate. There is no sign, yet, that they are willing to do so.

But the claim of victory is still important, for it represents a test for the president, too. His government has been consumed by war to the detriment of other things, notably basic human rights. President Rajapakse is a former human-rights activist who in 1990 called on donors to link aid to human rights and told parliament: “We are prepared to go to any lengths to save human rights from this government.” Now he stands accused of the very abuses he criticised. Defeating the Tigers might allow him to show his government in a better light.

That would mean, first, offering the Tamils genuine self-government. A system of devolution exists but has not been implemented. The system is feeble—Pillayan describes it as “just a start”—but there is little excuse for withholding it now there is an elected council in the east, home to Sinhalese and Muslims as well as Tamils.



Next, it would mean tackling neglected economic problems. The country is showing signs of a wage-price spiral, with annual inflation touching 26%, labour unrest and a threatened general strike. The convener of a teachers’ union, the delightfully named Joseph Stalin, says teachers are refusing to mark exam papers. The central bank is trying to break the wage-price cycle by a credit squeeze but its efforts are being undermined by government spending on the war. The budget deficit is 9% of GDP and there is pressure to spend even more on roads, canals, hospitals and Tamil-speaking nurses in the war-ravaged east.

Most important, improving the government’s reputation means allaying political and human-rights concerns. The Sinhalese, some 80% of the population, are Buddhists, who pride themselves on tolerance and calm. In his white costume, scarlet scarf and sandals, President Rajapakse cultivates the image of a beneficent guru. Yet the war has hardened attitudes. Criticism of it is called treason. “I’ve never seen the country so polarised,” says Paikiasothy Saravanamuttu, the head of the Centre for Policy Alternatives, a think-tank.

The press has been a bellwether. Basil Rajapakse, another of the president’s brothers, who is his chief adviser on domestic politics, says—unreassuringly— that the government does not want a law on censorship “but a voluntary self-control”. Accusations of harassment are frequent. This week a journalist from the Sri Lankan Press Institute, which had just launched defamation proceedings against a government-controlled newspaper, was attacked by club-wielding thugs, while travelling with a British diplomat, who was also clubbed. Late last year the International Press Institute put Sri Lanka on its watch-list of countries where the media’s situation is precarious, along with Russia.

More subtly, politics seem to have become less open and accountable. The reins of power have been drawn into the hands of the three Rajapakse brothers. In a region where democratic dynasties are common, the Rajapakse clan is unusual. It does not hail from the traditional English-speaking elite that produced Sri Lanka’s other presidents. Mahinda, from Hambantota, represents the rural south, the Buddhist provincial bourgeoisie, rather than the urban elite. To offset weak traditional loyalties, he has curried favour by lavish ministerial appointments. Sri Lanka has a huge, 108-strong cabinet. One minister resigned, saying his ministry should be abolished since it had nothing to do.

This has worrying consequences. Democratic Sri Lanka, which suffered more than most from the 2004 tsunami, has the sort of relations with international agencies you would associate with Sudan. In May it lost its seat on the United Nations Human Rights Council (not a body demanding the highest standards:

Russia, Cuba and Saudi Arabia are members). America's State Department has cited credible reports of government involvement in extra-judicial killings, and complicity in the recruitment of child soldiers by its allies. Sri Lanka's mission in Geneva responds to criticism by calling the former head of the UNHRC, Louise Arbour, unqualified to monitor human rights in the country. This dispute is self-defeating. Under a trade deal with the European Union called GSP-plus, Sri Lanka's garment exports (its second-largest source of foreign exchange) enjoy duty-free access to the EU. But GSP-plus hinges partly on human rights. Sri Lanka risks losing its privileges.

The president was elected on a platform of getting tough with the Tigers. But that was thanks partly to the boycott imposed by the Tigers themselves. Hardline governments, they reckon, end up helping their cause by driving even moderate Tamils into their clutches. Mr Rajapakse has driven the Tigers from the east, held an election there and claims to be closing in on victory. Yet the costs have been enormous and if the Tigers refuse to negotiate, there seems to be no alternative strategy to one entailing more bloodshed. Asked about this, Mr Rajapakse says the Tigers will be forced to talk—and, in a gesture he uses when nettled, shoves his bare feet firmly back into his sandals.

Economist.com WORLD ASIA

Kashmir

Land and blood

Jul 3rd 2008 | SRINAGAR
From The Economist print edition

The independence campaign flares up in a row about land for Hindu pilgrims

FIRE crackers and scattered cheering dotted the night on July 2nd in Srinagar, as Kashmiris celebrated a rare victory over the Indian government. Hours earlier, after a week of popular and violent protests, Kashmir's government had rescinded a gift of protected-forest land to Hindu pilgrims. In response, local Muslim separatists called off the protests they had organised. But after this triumph, which followed a year or so of relative calm in the troubled valley, fresh agitation seems likely.

Indeed, it may well spread beyond Kashmir and go national. On July 1st India's main opposition, the Hindu-nationalist Bharatiya Janata Party (BJP), called for a nationwide strike to put pressure on the state government—which, like India's central government, is a coalition led by the Congress party—to reverse its reversal. Sticking up for Hindu pilgrims—hundreds of thousands of whom flock to a cave in Kashmir each year to pay homage to a giant icicle they revere as an incarnation of the god Shiva—is staple fare for the BJP. So is sticking it to uppity Muslims.

Reuters



A pilgrim's rocky progress

As BJP leaders issued their call in Delhi, 80 people were injured in rioting by Hindu activists in Jammu, the southern, mainly-Hindu, part of India's only Muslim-majority state. With a general election due by next May and Congress in trouble on the back of soaring inflation and other woes, the contretemps is a godsend for the BJP.

It is also handy for Kashmir's separatist leaders. The 19-year-old freedom fight has cost over 40,000 lives, by the Indian army's count, and at least twice that by the separatists'; but the current death-rate, at a bit under 100 a month, is at an all-time low. That, and internal feuding, has taken the wind out of the separatist movement.

Fighting has flagged partly because Pakistan, which like India holds part of the historic kingdom of Jammu & Kashmir and claims all of it, has greatly reduced its former support to the insurgents. At the same time, Kashmiris seem increasingly resigned to the status quo. Some still hanker after the accession to Pakistan they feel was their due at partition in 1947; probably a greater number want outright independence. But many feel they have lost the battle. Turnout in local elections, which the separatists boycott, is increasing. By rallying support for their cause, separatist leaders may hope to dent turnout at the next state election, due by November.

Hence the vigour with which they pounced on the government's decision to grant 99 acres (40 hectares) of land to a Hindu body that manages the icicle pilgrimage. This, it was explained, was to help provide temporary shelter for more than 400,000 devotees who visit the icicle shrine, a cave at Amarnath in south Kashmir, each year. Yet the separatist chiefs preferred to see it as a brazen effort by the government to shift Hindus into the Muslim-dominated Kashmir valley.

Thousands agreed. Beginning on June 29th, the state capital, Srinagar, and the rest of the valley saw their biggest protests since the early-1990s, when the insurgency was at its height. Five people were killed and hundreds injured in clashes between the army and stone-throwing youths. In this time of strife, two of the biggest of Kashmir's many separatist factions, split over whether to negotiate with the government, were reported to have reunited.

Also on June 29th, after noting which way the wind was blowing, Congress's main local ally, the People's Democratic Party, quit the state government. Reduced to a minority, Congress is now looking for other allies to help it to hobble through to the polls later this year. The gleeful separatists are meanwhile plotting protests against the occupation of vast tracts of Kashmir by the army.

It may not stop there. Defying an unofficial curfew and a tear-gas bombardment by soldiers nearby, several thousand men gathered in Srinagar's main mosque on July 1st. Despite a dozen huge green Pakistani flags hoisted above the throng, the speeches they heard, from local religious and political leaders, were mainly for independence. "The land-transfer deal has brought so many issues to light," said one congregant, a local university professor. "In Kashmir, people are angry."



WORLD ASIA

Homosexuality in India

Glad to be gay (but a bit shy about it)

Jul 3rd 2008 | DELHI
From The Economist print edition

Where Victorian values and repressive laws still hold

EPA



Out of the closet, at least

THERE were no half-naked dancers, pink floats, or sailor boys locked in clinches; but India's gay-pride parade was ground-breaking enough without them. Several hundred men and women, waving rainbow flags, danced, stamped and sang their way through the city centres of Delhi, Bangalore and Kolkata (Calcutta) on June 29th—the first such national event in this conservative country. The parade was lent a uniquely Indian flavour by flamboyant cross-dressing *hijras*, known as eunuchs, although many modern *hijras* are gay men who feel alienated by mainstream society. Though *hijras*, once trusted courtiers of the Mughal emperors, have a well-established identity in India, gay men and women do not; indeed the practice of homosexuality is illegal, punishable with ten years' imprisonment.

Many of those who paraded under heavy monsoon clouds in Delhi said one of their main motives was to campaign for the repeal of that law, Section 377 of India's penal code, which deems homosexuality an "unnatural sexual offence" alongside bestiality. They say the section, drawn up 150 years ago by the British, is today routinely used by the police to harass and blackmail homosexuals, even if few are arrested. Delhi's High Court is currently weighing a petition against Section 377 brought by an umbrella group of Indian NGOs. "I feel we're living under the shadow of the Victorians," shuddered one young man, as beside him a group of *hijras* in hot pink saris broke into Bollywood-style pelvic thrusts. He might have added that he was also living under the shadow of his mother, who, he feared, would soon start introducing him to suitable girls. "I suppose then I will have to come out."

Despite a burgeoning gay scene in India's big cities, many Indian homosexuals worry more about exposure to their families and colleagues than about the law. "My brother knows; my mother doesn't," says Pankash, a 23-year-old year-old student who likes to be known as Tina when he goes on dates dressed as his glamorous alter ego. Though he was not incognito on Sunday, many of his fellow paraders were. Waving placards with slogans such as "Gay and loving it", many still wore paper masks, lest they were "outed" on television.



Economist.com WORLD ASIA

Malaysia

Here we go again

Jul 3rd 2008 | KUALA LUMPUR
From The Economist print edition

Allegations against Anwar Ibrahim may backfire on the government

EPA



Anwar on the counterattack

IN FEW countries does the word "sodomy" evoke a sense of political déjà vu. Malaysia is one. On June 28th a male volunteer working for the political campaign of Anwar Ibrahim, the leader of the opposition coalition, lodged a police report accusing him of sexual assault. Mr Anwar immediately called the accusation a "complete fabrication" and took refuge in the Turkish embassy, claiming that the government and police could not guarantee his safety. The government found itself in an awkward fix: its relations with the Turkish government were tested; and it had to declare that the safety of its main political rival was of the utmost importance.

When Mr Anwar left the embassy the next day, in a throng of press and supporters, he claimed that the accusation was a diversionary tactic. He said it was meant to derail announcements that he would be standing in a by-election, and that four members of parliament from the ruling Barisan Nasional (BN) coalition were about to defect to his side. In elections in March, the opposition made sweeping gains. Since then, a ban on Mr Anwar's standing for political office has expired, and he has said he is poised to topple the government as its MPs jump ship.

Whatever the motive for the allegations against Mr Anwar, or for his against the government, he seems for the moment to have the political initiative. This is partly a tribute to his political skills; but another factor is the sympathy, or at least indifference, of the Malaysian public, which hoped it had heard the last of sodomy in public life. The term entered the Malaysian political lexicon in 1998, when Mr Anwar was accused of sodomy and of corruption during the tenure of the then prime minister, Mahathir Mohamad, whom Mr Anwar served as deputy.

The sodomy accusation was widely believed to be politically motivated, and therefore untrue. The country found itself divided and appalled. But the nature of the alleged crime was scarcely an issue. What provoked outrage were the seemingly untrammelled powers of the prime minister, the dubious role of the judiciary and the blatant bias of the press. Mr Anwar served six years in prison before the sodomy (but not corruption) verdict was overturned in court. Yet perhaps the biggest victim of the episode was Dr Mahathir's legacy.

Mr Anwar was freed from jail early in the tenure of Abdullah Badawi, Dr Mahathir's handpicked successor (and now, butt of his fierce criticism). For many this was a happy conclusion to a lurid episode, not necessarily out of any deep affection for Mr Anwar but because what was widely seen as an injustice had at last been corrected. Sodomy, it was hoped, could be forgotten. Mr Anwar was yesterday's man.

All that changed with the March 8th election. The BN suffered its worst-ever electoral result and MrAnwar leapt back to the forefront of politics. The election could be read as a vote against BN rather than for Mr Anwar's disparate coalition. But he has since been portraying himself as prime minister in waiting. The sluggish pace of Malaysian politics has accelerated, and the momentum has been dictated largely by the opposition.

Mr Anwar still polarises opinion. A charismatic "comeback kid", he outshines his rivals in oratory and spin. But he remains an enigma. Some see a genuine democrat, admired by Western liberals. Others recall his youth as an Islamist firebrand, and doubt the sincerity of his transformation. Others see him as simply an ambitious opportunist. The confusion may be helpful: his coalition includes secular liberal democrats, a Malay Islamist party and a mostly ethnic-Chinese party. Mr Anwar is the glue that holds the odd mixture together. Without him it is hard to imagine how the coalition could continue to function or challenge for government.

Since the elections Malaysians have shown that they can cope with rapid change but the recent events have come as a shock. The word “bewildered” litters the Malaysian blogosphere. Conspiracy theories swirl but government ministers have denied any link with the accuser. He himself is in hiding. His family deny he has the backing of the government.

Mr Anwar and his supporters, however, have produced pictures of him with various people linked to the government, including an aide to Najib Razak, Mr Badawi’s deputy and heir-apparent. Mr Najib is enmeshed in scandal himself. One of his advisers is among those accused of the murder of a Mongolian woman. Mr Najib denies any involvement in the case, and he and his wife have denied claims made late last month that she was at the murder scene. But it has at least given Mr Anwar’s camp mud to sling back at his enemies. In 1998 Mr Anwar’s accusers failed to make the charges stick in the court of public opinion. That stands him in good stead as Malaysia hunkers down for an extended, unwanted, repeat performance.

Australia's aborigines

Tough love

Jul 3rd 2008
From The Economist print edition

This time "white paternalism" might actually be doing some good

Get article background

WHEN Sue Gordon was four, in the late 1940s, the authorities took her from her aboriginal community in outback Western Australia, put her on a train to Perth and handed her over to a Christian charity home. As a mixed-race child, she grew up as one of Australia's "stolen generations" ordered to obliterate her aboriginal heritage. Now 64, and a juvenile-court judge, Ms Gordon has just finished assessing an equally controversial government takeover of aboriginal lives. And she is surprisingly impressed.

After a report in June last year revealed widespread aboriginal violence and child sexual abuse in the Northern Territory, John Howard, the former conservative prime minister, ordered police and the army to take control of 60 remote indigenous communities. Aborigines make up 29% of the federal territory's population, compared with 2% nationally. Mr Howard's measures included compulsory health checks on children, confining the spending of welfare money to food and clothes, and the suspension of the communities' rights to grant permits to visitors.

Critics at the time blasted the "emergency intervention", as it was called, as a draconian return to the white paternalism that aborigines had fought for generations. But after visiting more than half the 73 communities eventually involved, Ms Gordon has found good progress in cutting violence and sexual abuse: alcohol and pornography have been banned, more children are going to school and police patrols have left more women feeling safer.

After Ms Gordon's report, Kevin Rudd, the Labor leader who succeeded Mr Howard in November, has undertaken to continue the A$900m ($864m) intervention exercise with another A$300m—but not indefinitely, as Mr Howard had planned. Since Mr Rudd's formal apology in February for past injustices, there is now pressure on aborigines to take advantage of the big-brother approach and secure self-reliant futures free from government.

Most of the Northern Territory communities stemmed from the land-rights movement of the 1970s, which allowed white Australia to absolve its guilt for kicking the original inhabitants off those lands. Government services did not follow the award of land, but alcohol, unemployment and social breakdown did. Ms Gordon is "aghast" at arguments that the communities should now be closed altogether and their people shipped out, just as in the bad old days. She accepts, though, that their survival can come only from developing their own economies with help from the private sector.

This is starting to happen already in resource-rich regions such as Western Australia. Andrew Forrest, whose company, Fortescue Metals, is making a fortune from that state's iron ore, has formed a trust to help mainly indigenous children. Mr Forrest told a recent forum in Kalgoorlie, a gold-mining city, that mining firms could eradicate aboriginal poverty by helping to create 250,000 jobs in the next decade. That may be optimistic. But Ms Gordon herself has set the example. She has raised almost half of the A$5m needed to buy the land where she lived in a charity home 60 years ago. She plans to build a place where she and other surviving inmates can care for each other in retirement.

 WORLD ASIA

Mongolia

Steppe change

Jul 3rd 2008 | BEIJING
From The Economist print edition

An election turns ugly

IN THE 18 years since the nation threw off Soviet domination and embraced democracy, Mongolian politics have been vibrant and even chaotic; but never violent. That suddenly changed after parliamentary elections on June 29th, when demonstrations over alleged vote-rigging turned into deadly unrest in the capital, Ulan Bator. Buildings and cars were set on fire, prompting the police to use tear-gas and rubber bullets and the president to declare a four-day state of emergency, with a night-time curfew, press restrictions and a ban on sales of alcohol. At least five people died in the violence on July 2nd and more than 300 were injured.

One of the buildings set ablaze was the headquarters of the Mongolian People's Revolutionary Party (MPRP), the ruling communists in the pre-reform era and still the dominant political force. Preliminary election results showed the MPRP taking as many as 45 seats in the 76-seat Great Hural, or parliament. The leading minority party, the Democratic Party, looked likely to take more than 20 seats. Nearly a dozen smaller parties appeared to have managed to win only three seats between them.

The losers were quick with accusations of electoral fraud, ranging from the stuffing of ballot boxes to the buying of votes, but their case is far from proven. Foreign observers, including some from the Russian and American governments as well as NGOs, have given the election passing marks. Luvsandenvev Sumati, director of Sant Maral, a Mongolian pollster, said his pre-election polls tallied closely with the preliminary results. Minor irregularities undoubtedly occurred but were "definitely not enough to sway the outcome".

Sanjaasurengin Oyun, Mongolia's foreign minister and a member of the minority Civil Will Party, said she barely managed to hold her seat in her own Ulan Bator constituency and was surprised at her shaky showing, but could not say fraud was a factor. She called the prime minister, the MPRP's Sanjagiin Bayar, a charismatic and able leader who had done a solid job of improving his party's public standing in the lead-up to the election.

She also cited the nation's new electoral system in which constituencies have been expanded and have multiple seats. This made it harder for minority parties to gauge their prospects. It has also worsened the post-election tension by slowing the count and official results. But she was optimistic the country's legal system could cope with any disputes and demands for recounts, once official results are declared.

Turnout was around 74% of the 1.6m eligible voters, a decline from the 81% recorded in the previous election in 2004. The campaign was dominated by the economy. The growth rate is near 10%, but Mongolia is grappling with inflation that last year passed 15%, as well as persistent poverty and unemployment. The new government also has to take a decision on a draft investment law that would allow large foreign mining firms to take big stakes in the country's vast gold and copper industries. Many of the smaller parties oppose this on commercial or environmental grounds. But the MPRP and Democratic Party support it, and are not likely to have trouble pushing it through.

Japan’s bureaucrats

A movable feast

Jul 3rd 2008 | TOKYO
From The Economist print edition

Illustration by Satoshi Kambayashi



A collision over cab collusion

THEY are called “pub taxis”. These fancy cabs drive Japanese bureaucrats home in the evening, provide a few beers, snacks and sometimes a discreet kickback (usually in the form of a shop voucher, sometimes good old cash). The practice has long been an open secret, but in the present irritable political climate, with speculation about an early election, it has now become a scandal. In June a lawmaker from the main opposition Democratic Party of Japan (DPJ) demanded an investigation. It revealed that more than 1,400 officials across the bureaucracy accepted such gifts, which are of questionable legality.

Government officials often work very late. Staff regularly stay past 3am to prepare ministers’ remarks for the next day’s Diet (parliament) session. Public transport ends soon after midnight, and they may take a taxi home with an expense-voucher. It is a perk of the job.

There are some 400,000 civil servants. They tend to live far from the expensive city centre, sometimes in government apartments. The taxi-ride may take more than an hour; the average fare is around $200. In 2006 one ministry (Transport and Construction) alone spent more than $20m on taxis. Most officials simply hop into one of the hundreds lining up outside the buildings in Kasumigaseki, Tokyo’s bureaucratic ghetto. But some drivers forge relationships, and lure customers with incentives. The bureaucrat will call the driver and arrange to meet; the incentive is a plush car, a few beers and a chance to doze rather than give directions. For the driver, one fare may bring most of a day’s income.

Exposing the taxi treats is serious politics. It lets the DPJ pose as the party of reform, battling the bureaucracy’s (overstated) profligacy and corruption. It also lets the DPJ attack proposals by the ruling Liberal Democratic Party (LDP) for increasing the consumption tax—by showing that the taxpayer’s money is anyway being misspent.

All sides can score political points by bashing bureaucrats. The LDP was quick to echo the DPJ’s fury. The finance minister and his deputy promised to return 20% of one month’s salary to take the blame—a classic Japanese symbol of official atonement. But when the Diet reconvenes in late August, the bureaucrats will still toil late and crawl into taxis for a long ride home, thirstily.

Zimbabwe

Africa's shame

Jul 3rd 2008 | JOHANNESBURG
From The Economist print edition

A Munich moment for the continent's leaders as President Robert Mugabe is let off the hook, again

Reuters



GATHERING in the Egyptian resort of Sharm el-Sheikh on July 2nd, the leaders of the African Union (AU) had an unprecedented opportunity finally to pull the plug on the disastrous regime of Zimbabwe's president, Robert Mugabe—or at least cast him into political outer darkness. To fortify themselves they had the world's condemnation of his farcical re-election on June 27th, which the opposition had to withdraw from due to violence and intimidation, ringing very loudly in their ears. They had the UN Security Council saying ahead of the poll that it could not be free or fair. They had the unprecedented verdict of their own observers, who had said that the result could not "reflect the will of the people". Even observers from a normally supine regional bloc, the Southern African Development Community (SADC), had said that the election could not be considered "legitimate".

So what did they do? The least possible. With Mr Mugabe in their midst, the AU leaders did concede that they were "deeply concerned" about the violence. But they responded by merely asking for mediation efforts to continue between Mr Mugabe and the opposition; these are led by South Africa's president, Thabo Mbeki, and have got nowhere. They also called for a government of national unity, without referring to whether such a government should be led by the man who won the sham runoff vote against no opposition on June 27th, or by Morgan Tsvangirai, the leader of the opposition Movement for Democratic Change (MDC), who actually won the first round of presidential voting in March. The AU's response was embraced by Mr Mugabe, which betrays exactly how much notice he is likely to take of any of it. With no penalties on the table for non-compliance, even the gentle suggestions emanating from Sharm el-Sheikh can be happily ignored.

A few of the continent's leaders did speak up. The vice-president of Botswana declared that the outcome of the election was not legitimate, and that Mr Mugabe and his government should therefore be excluded from AU and SADC meetings until a political solution is found. He was echoing similar words from Raila Odinga, Kenya's prime minister, whose own victory at the polls was stolen a few months ago. A group of respected African elders, including Nelson Mandela, Desmond Tutu and Kofi Annan, had asked for the AU to provide "leadership, wisdom and moral courage" by stating that the results of the runoff were illegitimate.

But these pleadings fell on deaf ears; for the AU leaders it was appeasement as usual. Many leaders on the continent are hardly paragons of democracy themselves, and so would never condemn a fellow

despot. One of the first to welcome Mr Mugabe to the AU meeting was Omar Bongo, who has ruled Gabon for decades; he quickly endorsed Mr Mugabe's election "victory". Others are still susceptible to the appeal of Mr Mugabe's anti-colonialist rhetoric. His spokesman will have done their cause no harm by saying that Westerners who condemned the election could "go hang a thousand times".

Meanwhile in Zimbabwe itself, months of horrific violence meted out to opposition supporters following the first round of the election have left deep scars on the country. Mr Tsvangirai withdrew from the race a few days before the runoff because of the repression and violence, which he says have left at least 86 people dead, thousands injured and arrested, and 200,000 others displaced. With no opposition, Mr Mugabe won 85% of the vote in the runoff, but many were forced to vote for him.

The experience of Malcolm (not his real name), a rural teacher from Mashonaland East, a stronghold of Mr Mugabe's ruling ZANU-PF, was fairly typical. He was also a polling officer, and explains how he was threatened the day before the runoff; like many other voters, he was forced to pretend he was illiterate on voting day so that he could be "assisted" by the police and ruling-party representatives in the voting booth. He recounts how those turned away because their names were not on the voters' roll begged for hours to be allowed to dip their fingers into ink, fearing retaliation if they could not display the mark proving they had voted. Although it took over a month for Zimbabwe's electoral commission to announce the results of the first round, which went against Mr Mugabe, it declared Mr Mugabe the winner of the runoff in less than two days.

The MDC's position appears muddled. Last week Mr Tsvangirai asked for the AU and SADC to help mediate a political solution based on the results of the first round. But on July 1st, Tendai Biti, the MDC's secretary-general who has been released on bail after being arrested upon his return to Zimbabwe, said that the runoff "totally and completely exterminated any prospects of a negotiated settlement", and that no discussions with ZANU-PF were happening. The next day, the opposition rejected the idea of a government of national unity, but said that it remains committed to negotiations towards a transitional government, provided the violence and the persecution of MDC leaders and supporters stop, political prisoners are released, militia bases and torture camps are disbanded, and security forces remain neutral.

Mr Mugabe, for his part, has said that he is willing to talk to anyone, safe in the knowledge that he now does so from a position of strength and with nothing to fear from the appeasing Mr Mbeki. On July 3rd South Africa, China and Russia were expected to defeat proposed UN sanctions targeted at members of Mr Mugabe's regime. Pressure on him from other sources might yet make his position more uncomfortable. For example, the German company that has supplied Zimbabwe with most of its banknotes for its hyper-inflated economy announced on July 2nd that it is ending its business with the country. In the grip of both a humanitarian catastrophe and an economic crisis, Zimbabwe is once again in limbo.

Somalia

Continuing to fail

Jul 3rd 2008 | NAIROBI
From The Economist print edition

Will Somalia ever get the peacekeepers it needs?

Get article background

AFTER months of delicate negotiations, Somalia's internationally recognised but feeble transitional government and its Islamist opposition agreed to work together to rebuild their ruined country. Under an agreement signed in neighbouring Djibouti in June, Ethiopia, which invaded Somalia in late 2006 to prop up the ailing secular-minded Somali government, was to withdraw its troops. Somalia's Islamists, who have been fighting an insurgency ever since, would stand their fighters down. It would have been a breakthrough for a country that has lacked a central government since the fall of its long-time dictator, Siad Barre, in 1991. But the deal was stillborn. Since then, Somalia has rotted away, a victim of international indifference and its own internecine history.

Somalia's more extreme Islamists have shown their contempt for the moderates by stepping up their attacks. The extremists are led by Sheikh Hassan Dahir Aweys, a wily former army officer who flirted with peace before rejecting it. He is aided by fighters loosely linked to the *Shabab* ("the Youth"), the armed wing of the Islamic Courts Union, which briefly ran most of the country in 2006, plus nationalist Somalis from disaffected bits of the powerful Hawiye clan and criminals flying a jihadist flag of convenience. And now al-Qaeda is sensing an opportunity in a country where it has previously got nowhere. Abu al-Libi, one of its top men, who escaped from the American Bagram prison camp in Afghanistan in 2005, has circulated a video on the internet calling on foreigners to fight alongside the Somali jihadists, with the aim of establishing a caliphate.

The extremists are helped by the continuing presence of Ethiopian troops. Most Somalis in Mogadishu, the capital, still resent them. After a recent retaliatory Ethiopian mortar attack, a Somali living in the capital described how he helped his neighbours: "We collected the flesh of their bodies that was stuck to the walls." Some 6,500 Somalis, many of them civilians, may have been killed since Ethiopia invaded early last year, though no one really knows the number.

The UN reckons that 2.6m out of 8m Somalis need help to keep fed and sheltered; some 1m have fled from their homes. That figure could rise with the recent failure of crops and the death of animals from drought. Spiralling food costs and the diving value of the Somali shilling have made things worse. Families are dying of hunger in camps for the internally displaced on the main road south of Mogadishu.



Somalia may be one of the most dangerous places in the world for one citizen to help another. Those who do often pay with their lives. Last week insurgents killed Muhammad Hassan Kulmiye, a brave local peace campaigner, and kidnapped a local head of the UN's Office of the High Commissioner for Refugees. Workers from several agencies, including Oxfam and the UN's World Food Programme, have been shot dead in recent weeks. Foreign aid workers from Kenya, Britain and Italy have been kidnapped and are still unaccounted for.

The United States had hoped that Ethiopia's intervention would secure regional stability by eliminating the more extreme Islamists. But it has succeeded mainly in pushing the more moderate ones together with the most belligerent. America's decision earlier this year to list the *Shabab* as a terrorist group has given American force commanders a green light to launch air strikes and send covert missions into Somalia. Some missiles fired from American submarines off the Somali coast have indeed killed Islamist insurgent leaders. But others have missed them—and killed Somali civilians instead.

Most moderate Somalis deplore the air strikes. So do most of the British, Swedish, Italian and Kenyan diplomats involved in Somalia (and based in Kenya's capital, Nairobi), as do many in America's own State Department. They say that the raids have weakened Somalia's moderates and strengthened the extremists.

The insurgency may be getting fiercer again. Government officials, including the president, Abdullahi Yusuf, an implacable foe of the hardliners, face frequent assassination attempts. Islamist insurgents have attacked towns and villages across the country, including some close to the border with Kenya. Its army has been deployed at the border and sometimes across it, but has been unable to stem the influx of Somali refugees. A complicated situation has been made worse by Eritrea, which supports Somalia's hardliners because they are killing Ethiopians, whom the Eritreans deem to be their enemy.

The only hope at present is for a robust international peacekeeping force to come in and allow the Ethiopians to withdraw. The UN Security Council has passed resolutions paving the way for its own blue-helmet mission. But this is unlikely to happen. UN-backed peacekeepers have an unhappy history in Somalia and furthermore the UN lacks resources. It took a lot of political pressure to get the Security Council to agree to send peacekeepers to Darfur, the blighted western region of Sudan; they have yet to arrive in the promised numbers months after they were due. Nor is it likely that the African Union will add to its few thousand peacekeepers, mainly Ugandans, in Mogadishu. Western diplomats working on Somalia say their reports make little impact on their governments back home. Despite the misery, the international will is lacking. So Somalia remains abandoned, lawless and too dangerous for most outsiders to operate in.



Africa and Coca-Cola

Index of happiness?

Jul 3rd 2008 | NAIROBI
From The Economist print edition

A bottle of Coke tracks change in Africa

AFRICANS buy 36 billion bottles of Coke a year. Because the price is set so low—around 20-30 American cents, less than the price of the average newspaper—and because sales are so minutely analysed by Coca-Cola, the Coke bottle may be one of the continent's best trackers of stability and prosperity.

"We see political instability first because we go down as far as we can into the market," says Alexander Cummings, head of Coca-Cola's Africa division. The ups and downs during Kenya's post-election violence this year could be traced in sales of Coke in Nairobi's slums and in western Kenya's villages. Events in the Middle East, such as the 2006 war between Hizbullah and Israel, can dent sales in Muslim parts of Africa, though anti-American feeling usually wears off quite quickly.

Coca-Cola says it is the largest private-sector employer in Africa. Its system of distribution, which moves the sugary drink from bottling plants deep into slums and the bush a few crates at a time, may employ around 1m Africans. A study at the University of South Carolina suggested that 1% of South Africa's economy was tied up, one way or another, in the distribution and sale of Coke. The company has been in Africa since 1928. Its outgoing global boss, Neville Isdell, grew up—barefoot, he says—in Zambia. Mr Cummings is from Liberia. In Africa, as elsewhere, the company has to defend itself from critics who accuse it of "mining water" for production, encouraging expensive and environmentally harmful refrigeration, and hurting local producers of juice and water.

At a macro-level, when Coke fails, the country whose market it is trying to penetrate usually fails too. Coca-Cola's bottling plant in Eritrea hardly works because the country's totalitarian government makes it impossible to import the needed syrup. The factory in Somalia sputtered on heroically during years of fighting but finally gave out when its sugar was pinched by pirates and its workers were held up by gunmen. Mr Cummings admits that Coca-Cola is "on life support" in Zimbabwe.

Still, if Coca-Cola's predictions are anything to go by, Africa's future is mostly bright. The company expects sales in Africa to grow by an annual 10-13% over the next few years, handily outstripping economic growth. The biggest markets will be in petro-economies such as Nigeria and Angola, and countries like Ghana and Kenya where a middle class is emerging. Kenya's citizens may like to know that, despite their country's many troubles earlier this year, Coca-Cola has invested $50m in a new bottling plant and $10m in new offices.

Israel's prisoner swaps

A dubious trade

Jul 3rd 2008 | JERUSALEM
From The Economist print edition

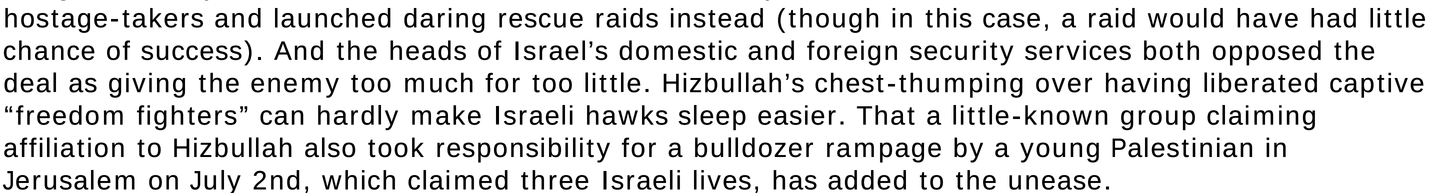
Politics overrides security advice for Israel's beleaguered prime minister

EPA



WHAT is the right price for a dead soldier? The question has gripped Israel this week after the government said that it had accepted a prisoner swap with Hizbullah, Lebanon's Shia militia.

Under the deal, Israel will surrender Samir Kuntar, a Lebanese who has been in jail since he killed three Israelis in 1979, as well as four other Lebanese prisoners and the remains of several more. Later on, it will turn over an unspecified number of Palestinian prisoners to Hamas, the Islamist movement that controls the Gaza Strip. In return it will get back Eldad Regev and Ehud Goldwasser, two soldiers whom Hizbullah kidnapped two years ago, sparking a five-week-long war, along with a report on the fate of Ron Arad, an air force officer whose plane was downed over Lebanon in 1986 and who was known to be alive until talks to release him broke down in 1988. Mr Arad has long been presumed dead, and the government says Mr Goldwasser and Mr Regev probably are too.



Some newspaper pundits praised the exchange as proof of how highly Israel values its soldiers, even when dead. Others mournfully recalled the glorious days when Israel refused to do deals with hijackers and hostage-takers and launched daring rescue raids instead (though in this case, a raid would have had little chance of success). And the heads of Israel's domestic and foreign security services both opposed the deal as giving the enemy too much for too little. Hizbullah's chest-thumping over having liberated captive "freedom fighters" can hardly make Israeli hawks sleep easier. That a little-known group claiming affiliation to Hizbullah also took responsibility for a bulldozer rampage by a young Palestinian in Jerusalem on July 2nd, which claimed three Israeli lives, has added to the unease.

But Ehud Olmert, Israel's prime minister, needed a victory. Corruption scandals, criticisms over his handling of the 2006 Lebanon war and pressure from the missing soldiers' families through the media had pushed Labour, the second party in Mr Olmert's governing coalition, to present him with a choice: face early parliamentary elections, or hold primaries within his Kadima party by September 25th. He chose the latter. Despite everything, if he notches up some successes before then he might still see off his rivals within Kadima.

The Lebanese swap, which could take place in the next fortnight, would be the first success. The next could be to close a deal with Hamas to exchange Gilad Shalit, a soldier it has been holding (alive) in Gaza for two years, for more Palestinian prisoners—possibly over a thousand, making it the most expensive such swap in Israel's history. Again, for a weakened prime minister, the pressure to get Mr Shalit back safely has been intense.

But the talks with Hamas, being mediated by Egypt, can go ahead only if a ceasefire that the two sides agreed last month holds. It has been breached almost since the first moment. Other militant groups in Gaza have launched a handful of mortars and rockets at Israel, provoking exasperation from Hamas, which seems unable to control them. Israel, for its part, has kept shut border crossings with Gaza that it was supposed to open, and several times Israeli troops have shot at Palestinians who strayed near the Gaza border fence, injuring at least one.

The third thing that might win Mr Olmert some points is the peace talks he recently launched with Syria. Direct talks last foundered in 2000, though the two sides were reportedly close to a deal in which Israel would return the Golan Heights that it occupied in 1967. The current talks have so far been indirect, with Turkish mediators shuttling between Israeli and Syrian officials in Ankara. But there is much speculation

that Mr Olmert may talk to or shake hands with Bashar Assad, the Syrian president, at a summit of European and Mediterranean leaders in Paris on July 13th.

That would be a small but significant gesture. But further progress would still be hard. Domestic opposition in Israel to returning the Golan, where about 17,000 Israelis have settled and many more take their holidays, is strong. Israelis want another sign of goodwill from Syria, such as returning the remains of Eli Cohen, an Israeli spy who was convicted and hanged in 1965. A Syrian with experience in unofficial "track-two" negotiations suggests that Israel could make its own gesture by relinquishing the Shabaa Farms, a small, unpopulated nub of territory on the Golan which Lebanon claims as its own. America has proposed that Israel hand it over to the UN. "It doesn't matter who it really belongs to," says the Syrian. "Give it up and you would kill two birds with one stone."

Iran's confrontation with the West

Dangerous games

Jul 3rd 2008
From The Economist print edition

Some scary noises, but maybe also some progress on the nuclear front

Reuters



Holding off the threat of Israeli air power

AS IS well known, one reason for the giddying rise in oil prices is the fear of a messy conflict over Iran because of its suspected ambition to build atomic bombs. The danger is not simply of a cut-off in supplies from Iran, the world's fourth-largest exporter, but of a prolonged threat to the wider Gulf region, which accounts for 40% of oil traded on the world's markets. Yet if everyone believed the warmongering noises coming from both Iran and its critics, the price of oil would be higher still.

Iranian newspapers, for instance, have reported plans by the army to dig some 320,000 graves near its borders, supposedly a humanitarian move to speed the disposal of enemy corpses and so “reduce the pain and hardship of the families of the soldiers who will be killed in any possible invasion of our country.” One commander advises that any invaders should equip themselves with artificial legs, because they will not be walking home.

In a more sober vein, the head of Iran's Revolutionary Guards, General Muhammad Ali Jafari, told interviewers that the danger of an American attack had risen in the waning months of the Bush administration, because of the “Republican hopelessness regarding the victory of their candidate.” Iran's response to aggression would be swift and decisive, said Mr Jafari, and could include strikes against Israel, strikes at countries hosting American bases in the Gulf, and exerting control over the narrow Strait of Hormuz, through which most of the region's oil flows to market. “Certainly if there is fighting the scope will be extended to oil, meaning its price will increase drastically,” he said.

Mr Jafari's remarks came in response to a string of what were seen in Tehran as provocative developments. These have included reports of massive Israeli long-distance aerial manoeuvres and revelations of a boost in covert American funding to Iranian opposition groups. There were also statements attributed to senior Israelis and Americans suggesting that the window for military action could close within a year, because by then Iran might already have developed a bomb, or improved its air defences sufficiently to deter any attack.

Yet both the Israeli and American governments distanced themselves from these provocative statements. Asked about an unnamed Pentagon official who hinted at an imminent Israeli attack in a television interview, a State Department spokesman said that if such talk were credible, the source should not remain unnamed. In fact, American diplomats are talking about resuming direct talks with Iran over Iraq, and even of sending the first American diplomats to Tehran since the 1979-81 hostage crisis. It was also reported this week that the Pentagon stopped the air force from deploying its newest fighter to the Gulf, the F22, for fear of causing “strategic dislocation” with Iran.

Amid the drums of war Iran, too, has been sounding a quieter *leitmotif* of compromise. On numerous occasions, senior regime figures have chastised the country's feisty populist president, Mahmoud Ahmadinejad, for stirring up needless trouble with his bellicose rhetoric. And in contrast to how previous international overtures were met in Iran, the most recent offer of a deal over the nuclear issue, presented last month by European diplomats, has prompted widespread public discussion and even positive official noises.

Ali Velayati, who was foreign minister from 1981-97, and remains a top adviser to Iran's Supreme Leader, Ayatollah Ali Khamenei, has publicly declared that Iran should accept the proposal, which calls for an initial six-week period of preliminary talks, during which Iran would forego any expansion of its enrichment programme in exchange for a freeze on new sanctions. The head of Iran's atomic energy agency has also weighed in, according to Iranian news sites, apparently telling the Iranian parliament's energy committee that the decision has already been taken to start the talks. It remains unclear, however, whether Iran would follow this with a full suspension of enrichment, which remains the condition set by America, Britain, France, Russia and China, the five permanent members of the UN Security Council, plus Germany for letting Iran off the sanctions hook.

Some naysayers believe this may simply be another Iranian stalling tactic, while others say it shows that the escalation of tensions, and the recent beefing up of sanctions brought by a European Union move to freeze dealings with Iran's biggest bank, is causing Iranian officials to blink. Iranian analysts prefer the view that their leaders, reckoning that dangers may ease following America's presidential election, simply wish to keep things calm until November.



Clarification: Morgan Tsvangirai

Jul 3rd 2008
From The Economist print edition

In our article on the United Nations and Zimbabwe ("Crimes against humanity") on June 28th, we said that "Morgan Tsvangirai, Zimbabwe's opposition leader, has called for the United Nations to send peacekeepers." This was expressed in an article under Mr Tsvangirai's name in the *Guardian* on June 25th. He subsequently said the article had not been authorised by him and that he wanted the UN to help "manage the transitional process" but he had not advocated military intervention "by the UN or any other organisation".

Spain

¿Crisis? ¿What crisis?

Jul 3rd 2008 | MADRID
From The Economist print edition

Illustration by David Simonds



Spanish voters are belatedly waking up to the extent of their economic problems—although the prime minister still denies them

SUCCESSES in soccer and politics do not always go together. Even as euphoric Spaniards revel in their team's Euro 2008 win on June 29th, they know that the real party, celebrating a decade of fizzy growth, is over. The Socialist prime minister, José Luis Rodríguez Zapatero, would prefer them to focus on sport, not the economy. But even though he was elected to a second term in March, his popularity is now tumbling, in line with the economy.

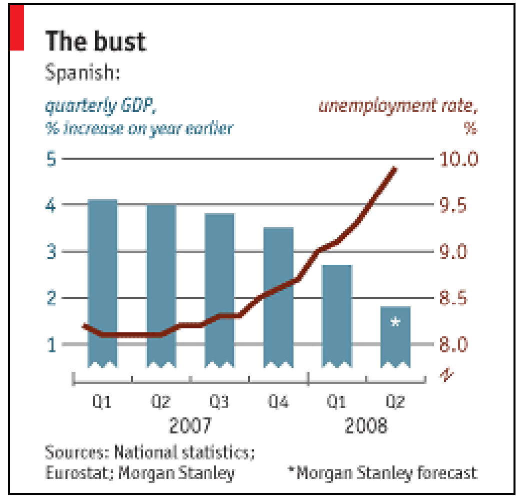
The litany of bad news has become interminable. Growth is slowing sharply and unemployment is rising. The housing bubble has burst and residential construction has seized up. Prices of petrol, electricity, food and a host of other things Spaniards buy have all gone up sharply, as (on July 3rd) did euro-area interest rates.

It is no surprise that half of all Spaniards now consider their personal financial position to be worse than in March. This may not be all Mr Zapatero's fault, but he is the man they are blaming. Striking truck-drivers caused chaos on the roads and left supermarket shelves empty for a week in June. The four-point lead that the Socialists had over the People's Party (PP) opposition in March has now evaporated.

It does not help that the government keeps denying that it faces a crisis. The finance minister, Pedro Solbes, refuses to utter the word "crisis" at all. Mr Zapatero told the daily *El País* that its use was "a matter of opinion". They are supported by Banco Santander's president, Emilio Botín, who compares the fraught state of the economy with a child's fever: dramatic, but short-lived. Yet crisis may be too bland a word: many economists think "recession" will soon be more appropriate. Mr Solbes admits that second-quarter growth will be below the first quarter's paltry 0.3%. His prediction of 2008 growth is now somewhere "below" 2%. On July 2nd a defiant Mr Zapatero told parliament he did not believe recession was coming.

In his first term, a smiling Mr Zapatero rode the crest of the economic wave, with a feel-good image of optimism and positive thinking. From regional devolution to gay marriage, he spread a message of goodwill to all. The economy was given little attention

as it turned in growth rates well above 3% every year. Cures for every social or political ill seemed possible, as there was plenty of money around.



Things started to go wrong when Spain's frothy construction industry began to deflate last year. A healthy budget surplus, a promise that the grey but trusted Mr Solbes would run the economy and a pledge to return €400 ($630) to every taxpayer helped the Socialists to win the election. In effect, Mr Zapatero got back before voters realised how bad things were. His €400 rebates will pump some €6 billion into consumers' pockets. Yet much of it has already been swallowed up in higher mortgage payments and soaring petrol and food prices. The budget surplus has gone. This year Mr Solbes promises only "almost balanced" accounts.

What else can Mr Zapatero do? He has no control over interest rates, international finance or commodity prices. More infrastructure spending is touted as one answer, but with the Socialists pledging not to cut social spending, it will mean either more borrowing or finding offsetting spending cuts. More privatisation may help, as will a cut in the numbers of bureaucrats and a freeze on senior civil-service pay—but the amounts are not huge.

What the economy really needs, says the Bank of Spain, is to rein in wage growth and make the labour market more flexible. Mr Zapatero has called on unions and employers to start talking. But Mr Solbes has said that making it cheaper to fire workers is not a priority. Cuts in corporate-tax rates have also been ruled out. Other supply-side reforms, for instance to education, will have little immediate impact.

On the political side, too, Mr Zapatero is set for a bumpy second term. The PP leader, Mariano Rajoy, has at last shifted his party towards the centre after a long ideological battle. His reward, according to one poll, was to become more popular than Mr Zapatero for the first time. Mr Zapatero heads a minority government that is seven seats short of an absolute parliamentary majority. The small nationalist parties from Catalonia, the Basque country and elsewhere hold the balance of power. They are already playing tough over supporting next year's budget.

If the economy offers him no respite, where can Mr Zapatero turn to boost his flagging image? Step forward the Basque regional premier, Juan José Ibarretxe, who has called a double referendum on talks with the armed separatists, ETA, and on a vague Basque "right to decide". Mr Ibarretxe, a nationalist, is pushing the limits of devolution and seeking votes in the regional election due this autumn. But he may also have handed a gift to Mr Zapatero. The referendum gives him a chance to be hard on ETA and devolution—both areas where voters thought he was too soft in his first term. Mr Zapatero has said he will get the referendum banned by the constitutional court before it can take place.

This is not the only example of Mr Zapatero's deciding that being tough can pay. Spain's immigrants, most of whom arrived in the past seven years, have accounted for a big chunk of the economy's growth. Now they are starting to lose their jobs. Immigrants make up 11% of the workforce, but half of those who are newly unemployed. The government is offering to pay them a lump-sum unemployment benefit if they go home. A plan to stop them bringing over parents or adult children may discourage new immigrants. Both measures appeal to voters who fret that immigration has been too rapid.

Mr Zapatero has spotted a problem that many Spaniards now confront for the first time, as they compete with immigrants for scarce jobs. In his second term, Spain's so far relaxed race relations may be tested. Fixing the economy would be the best answer. But getting tough on immigrants may prove an easier way to stay popular than promoting unloved economic reforms.

France's Socialists

Left and ultra-left

Jul 3rd 2008 | PARIS
From The Economist print edition

A party that ought to be doing better looks for a new leader

AFP



Besancenot, anti-capitalist crusader

THIS should be a fertile time to be a French Socialist. Global capitalism, demon of choice for the French left, is in chaos. President Nicolas Sarkozy's popularity has collapsed. France is about to rejoin the military command of NATO, seen by the left as a tool of Anglo-Saxon hegemony. And yet the French Socialist Party is busy tearing itself apart.

In November François Hollande, the party leader, is due to step down. Elbowing towards his seat are half a dozen candidates who have been publishing their "contributions" ahead of the party congress. The front-runners are Mr Hollande's ex-partner and a defeated presidential candidate, Ségolène Royal; Bertrand Delanoë, mayor of Paris; and, in a late surge, Martine Aubry, mayor of Lille and architect of France's 35-hour week.

Given that the Socialists have lost three presidential elections in a row, some modernising might seem in order. The party has boldly given up a reference to "revolution" in its founding principles. There was a hint of renewal when Mr Delanoë, flush from his Paris re-election in March, called himself "liberal", a term of abuse inferior in France only to "ultra-liberal". But he hastily insisted he was "both liberal and socialist" and his liberalism was mostly "political"—eg, backing adoptions by homosexual couples.

Ms Royal's pitch is an odd mix of old-style socialism (more workers on company boards) and surprising fiscal conservatism (a lone promise not to boost the tax take). In a recent speech to rock-star applause in Paris, she cited Engels and castigated Mr Sarkozy for favouring "the France of Falcon jets", but called for an open mind over an alliance with the political centre. Farther left sits Ms Aubry, who has support from the teaching and public-sector backbone of the party. Her bid calls for a higher minimum wage and a tax on international capital flows, but also argues in quasi-Blairite tones that "to redistribute wealth, it must first be created".

As rival leaders grope for a definition of the centre-left, however, a political gap is opening up to their left. One far-left politician has been grabbing attention: Olivier Besancenot, a youthful-looking, T-shirt-wearing postman and former Trotskyite presidential candidate. In a startling recent poll, he was judged "the best opposition to Nicolas Sarkozy", beating, in order, all the old guard: Mr Delanoë, Ms Royal and Mr Hollande.

Appealing to anti-market hostility in France, the new darling of media talk-shows is launching a "New Anti-Capitalist Party", to "prepare a radical revolutionary transformation of society" and "the end of capitalism". Mr Besancenot's ascent, and ready populist message for troubled times, is starting to worry the Socialists. Needless to say, the right, itself hurt for so long by the far-right National Front, can scarcely conceal its glee.



Corruption in Romania

In denial

Jul 3rd 2008 | BRUSSELS AND BUCHAREST
From The Economist print edition

The European Union conceals Romania's backsliding on corruption

HOW bad is corruption in Romania? Somebody well-placed to answer is Willem de Pauw, a Belgian prosecutor who is a veteran European Union adviser on the matter. Last November he wrote a report that concludes: "instead of progress in the fight against high-level corruption, Romania is regressing on all fronts…if the Romanian anti-corruption effort keeps evaporating at the present pace, in an estimated six months' time Romania will be back where it was in 2003."

This report has not been published (it is now available here). The European Commission's report in February was a lot softer. "In its first year…Romania has continued to make efforts to remedy weaknesses that would otherwise prevent an effective application of EU laws, policies and programmes. However, in key areas such as the fight against high-level corruption, convincing results have not yet been demonstrated."

That falls far short of admitting that Romania's authorities are wilfully failing to co-operate. Some of Mr de Pauw's most striking examples did not appear in the official report either, or were buried in footnotes. Mr de Pauw confirms his authorship but refers inquiries about it to the commission. Officials say he was consulted on the issue. Their February report, they add, was a "factual update", not an assessment of Romania's progress. That will come in a fuller report later this month.



It would be encouraging if this included some of Mr de Pauw's points. One hot example is the cases that courts have sent back to prosecutors since Romania's constitutional court struck down an anti-sleaze law. Mr de Pauw's report said that "basically all" high-level corruption trials had been rebuffed by courts, which it was "statistically impossible to attribute [to] the coincidental occurrence of procedural mistakes in individual cases. Other factors than legal-procedural considerations have clearly played a major role." He added that "the Romanian judiciary and/or legal system appears…unable to function properly when it comes to applying the rule of law against high-level corruption. Indeed, more than five years after the start of Romania's anti-corruption drive, the public is still waiting for one single case of high-level corruption to reach a verdict."

Events also support Mr de Pauw's warning that Romania could soon regress to the level of 2003. Take the case of Adrian Nastase, a former prime minister charged with several counts of corruption and bribery. He has now been exonerated by the parliamentary committee on legal affairs. A lobby group, the Initiative for a Clean Justice, complains that "we are witnessing the transformation of parliamentarians into judges and of the judicial committee into an extraordinary court." A full parliamentary vote on the committee's recommendation has been postponed until after the EU's July report. But Mr Nastase and his supporters are already considering a presidential bid in 2009.

In retrospect, the EU relied too much on individual politicians to back Romania's anti-corruption drive, notably Monica Macovei, a much-admired justice minister. She was fired soon after Romania joined the EU in January 2007. Membership made the political elites feel they were off the hook. Mr de Pauw offers a bleak verdict. "Many of the measures that were presented, before accession, to be instrumental in the fight against corruption, have been deliberately blunted by parliament or the government immediately after accession…all major pending trials concerning high-level corruption, started just before accession and only after many years of hesitation, have now been aborted and are, most probably, definitely abandoned for all practical purposes." He also cites the weakening of the role of the National Integrity Agency, meant to limit politicians' conflicts of interests and verify their assets, and also amendments to

the penal code before parliament that will “fatally affect” the investigation of corruption.

All this, he says, shows “the intense resistance of practically the whole political class of Romania against the anti-corruption effort”. Mid-level Eurocrats, as well as some foreign diplomats in Bucharest, agree. The problem is that countries such as France pushed to get Romania into the EU early for their own reasons, whether financial or geopolitical. And the political pressure may now be to cover up, not expose, the problem. If the EU’s July report on Romania is as anodyne as the previous one, suspicions will only grow.

Nordic defence

Pooling resources

Jul 3rd 2008 | COPENHAGEN
From The Economist print edition

The Nordics get chummier as costs mount—and more think about NATO



AFP

A modern Viking

DESPITE their Viking warrior past, Nordic countries are keen peacekeepers. Under the auspices of the United Nations, the European Union, NATO and the OSCE, their soldiers are in Afghanistan, Kosovo, Lebanon and Chad. Not that they are all in the same places. The mix of defence clubs to which the five belong dictates their involvement. Norway and Iceland are NATO stalwarts but not in the EU. The reverse holds for Sweden and Finland. Denmark is in both clubs, but cannot take part in EU missions because of its defence opt-out from the Maastricht treaty. (Countries can still join missions under arrangements for "partnerships" or "observer status".)

Some military and political leaders want the Nordics to co-operate more. Sten Tolgfors, Sweden's defence minister, has suggested sharing airbases with Norway. And he says that if Norway replaced its ageing F-16 fighters with Swedish-made Gripens, rather than the Joint Strike Fighter, Nordic co-operation would benefit (as would Sweden's defence industry).

The army chiefs of Finland, Norway and Sweden have published a report identifying 140 areas of possible co-operation. Yet their interest in it is largely about costs. "Defence-sector purchasing power has been gradually reduced and there is a growing imbalance between defence costs and budgetary allocations," the military men wrote. This dig at the politicians was blunt but unsurprising. More missions abroad and rising costs of kit have left all Nordic forces cash-strapped.

Norway's are struggling to trim their costs by some 1.1%. An official commission in Sweden has suggested cuts in purchases of anti-aircraft defences, tanks and fighter aircraft. This has yet to be approved by the government, but Hakan Syren, the senior Swedish commander, worries that "the armed forces are being forced to lower their ambitions when it comes to their ability to repel extensive military operations that threaten Sweden."

One big consideration is the growing threat of Russia, which last year resumed ostentatious long-distance bomber flights close to northern Europe. Sweden and Finland may yet seek refuge in NATO. Sweden's four-party coalition is divided, and the issue is officially off the agenda for now. But some politicians, including Mr Tolgfors, now argue that NATO is a natural source of Swedish security. "The Nordic countries cannot by themselves generate sufficient political and military weight," he says. If Finland, Russia's immediate neighbour, feels twitchy enough to think about joining NATO, that may ignite debate in Sweden. That could in turn foster closer co-operation among all five Nordic countries—though even full NATO members are not always good at this.

Georgia, Abkhazia and Russia

Tales from the Black Sea

Jul 3rd 2008 | SUKHUMI AND TBILISI
From The Economist print edition

The Abkhaz and the Georgians have reason to resent each other—but both need to rebuild trust if they are to have a prosperous future

AT MIDDAY Ochamchira, in Abkhazia, is almost empty. A derelict cement tower and rusty fairground wheel are the backdrop to an empty stretch of Black Sea coast that was once the Soviet riviera. The ageing owner of a bar is reading a book of Soviet recipes, but his only customer is a woman who downs her vinegary red wine and leaves. "This time 15 years ago people were queuing outside," he says. Then there were 25,000 residents; today 3,000 are left.

The ethnic conflict between Georgia and its breakaway enclave, Abkhazia, was one of many detonated by the collapse of the Soviet Union. Recently, this patch of land, in law part of Georgia but in effect controlled by Russia, has become a new frontier between Russia and the West. Two months ago Georgia and Russia came close to war. Russia accused Georgia of preparing a strike on Abkhazia, mobilised paratroopers and artillery to join its "peacekeepers", and shot down a Georgian drone. Hotheads in Tbilisi and Moscow said that war was all but inevitable.

Diplomatic intervention by Europe and America staved it off, but tensions remain high. This week bombs exploded in the Abkhaz town of Gagra and the capital, Sukhumi, prompting Abkhazia to close its border with Georgia; and Russia reopened a sea route between Sochi and Gagra. On July 2nd a bomb ripped through an apartment block in Sochi, host of the 2014 winter Olympics. The Russians make no bones over linking trouble in Abkhazia to Georgia's hopes of securing NATO membership, which they strongly resist. But even as Georgia and Russia argue, nobody pays much heed to the Abkhaz themselves.

The Abkhaz and the Georgians belong to different ethnic groups but have shared this bit of Black Sea coast for centuries. When the Bolsheviks occupied Georgia, Abkhazia was given the status of a Soviet republic. Only in 1931 did Stalin (a Georgian) turn Abkhazia into an autonomous region of Georgia. Later his secret-police chief, Beria (also a Georgian, born in Abkhazia), resettled Georgians from the western part of the country in Abkhazia, tipping its ethnic balance further in favour of Georgians. Abkhaz schools were shut and the language was banned.

When the Soviet Union fell apart, various ethnic time-bombs planted by Stalin across the Caucasus began to go off. In August 1992 Georgia, itself in near anarchy, began a war in Abkhazia. Nominally under the rule of Eduard Shevardnadze, the country was run by nationalist warlords who recruited criminals to their armies. These troops pillaged Abkhazia, defeating the ill-armed Abkhaz. When the tide of the war turned and the Abkhaz, helped by Chechens and Russian mercenaries, stormed back, they massacred ethnic Georgians. Atrocities were committed on both sides, and some 250,000 of the pre-war Georgian inhabitants (who accounted for 45% of the total population) were forced out through ethnic cleansing. But the Abkhaz look back on the conflict as a war of independence and show little sympathy for Georgian refugees. Their mistrust of Georgia is boosted by Russia's anti-Georgian propaganda.

Russia, which fanned the conflict first by encouraging the Georgians, then backing the Abkhaz, has throughout played a highly dubious role. It claims to be an impartial peacekeeper, but it has strong vested interests. The Russians have ignored sanctions on Abkhazia meant to force the Abkhaz to take back their refugees, and have also given most Abkhaz Russian passports that let them travel abroad. With 90% of the population enlisted as "Russian citizens", watching Russian television, using Russian money and receiving Russian pensions, Abkhazia is barely autonomous. And though the Russians often talk about Kosovo as a precedent, they do not really want to see Abkhazia's independence.



The Abkhaz realise the dangers of assimilation into Russia and are wary of Russian nationalism. When Russia tried to dictate their choice of president, Abkhaz voters picked his rival. Yet even if integration with Russia seems unappealing, to many the idea of being part of Georgia is worse. “At least Russia did not fight against us,” says Stanislav Lakoba, head of Abkhazia’s security council. He adds that Georgia’s hard line and Europe’s indifference have driven Abkhazia into Russia’s arms.

The Abkhaz also know that the only reason for the sudden interest in their plight is Russia’s increasing belligerence. But Sergei Bagapsh, the de facto president, has ruled out replacing or even altering the Russian peacekeeping force. “Our interests will be represented only by Russia,” Mr Bagapsh said after meeting Dmitry Medvedev, Russia’s president, recently.

Some of the blame for this situation rests with Georgia’s president, Mikheil Saakashvili. When he swept to power in 2004, he did not use his popularity to apologise for Georgia’s past actions or disown the legacy of his predecessors. By late 2004, Georgia was getting closer to a deal with Russia and a no-use-of-force agreement with Abkhazia, but neither document was signed. Mr Saakashvili said that “we are not inviting separatists to Georgia, we will ourselves return to Abkhazia.” His populism irritated the Abkhaz, as did his decision to banish Irakli Alasania, the only man the Abkhaz side trusted as a negotiator, as ambassador to the UN in New York.

In 2006 the Georgians forced their way into the upper Kodori gorge, violating a 1994 peace agreement. They said they had to clear the area of a local warlord. But Paata Zakareishvili, a Georgian analyst, believes he could have been nabbed in Tbilisi. Ruslan Kishmaria, who oversees Gali, a region where 50,000 Georgian refugees spontaneously returned after the war, says Georgia refuses to let the UN verify their return. Georgian television channels disseminate false reports of Georgians being assaulted from the Abkhaz side. Earlier this year the UN secretary-general said that “inaccurate reports originating in the Georgian media and occasionally the Georgian authorities…have contributed to growing distrust and insecurity.”

In the circumstances, it is hardly surprising that Mr Saakashvili’s latest peace plan, offering Abkhazia unlimited autonomy, was dismissed as propaganda by the Abkhaz. Mr Saakashvili announced it on Georgian television (which is blocked in Abkhazia). When it was delivered to the Abkhaz, they refused to touch it.

Georgia talks of developing free-trade zones in Abkhazia, but is yet to lift sanctions that do not work anyway. Mr Alasania, whose father was killed in the 1990s war, says that “the key to this conflict lies not in Washington or Moscow but in Tbilisi and Sukhumi…we have to take the first steps towards reconciliation.” Rebuilding trust between the two sides may take years—and even then it may not lead to full reintegration of the country. But if Georgia wants to stay democratic and prosperous, it has no other option. And if they want to preserve their sense of identity, the Abkhaz must do their bit too.

Charlemagne

The French connection

Jul 3rd 2008
From The Economist print edition

Why Europe is nervous about Nicolas Sarkozy's stint in the chair

Illustration by Peter Schrank



CERTAIN phrases invite disbelief. In the field of love, "this is not about you". In criminal justice, any testimony that begins "to tell the truth". In the European Union, France always earns instant suspicion whenever it swears to be "selfless" and to "put the general European interest first".

This is one reason why so many Europeans were feeling nervous on July 1st, when France took over the six-monthly rotating presidency of the EU. But there are others. Most obviously, the members do not trust the French president, Nicolas Sarkozy, to be chairman of the club. For all the welcome energy he brings (especially after the sullen paralysis of Jacques Chirac's final years), the suspicion is that he is not interested in Europe as a forum in which 27 leaders debate and come to an agreement. Instead, comments one EU diplomat, Mr Sarkozy seems to see Europe as a backdrop for his own bilateral deal-making.

Moreover, most other members of the EU club mistrust France's voters, who seem to take a dramatically different view of the world from theirs (look at polls measuring French opinions of the free market or of the role of the state). Mr Sarkozy promises to use the French EU presidency to show that Europe can tackle everyday concerns of citizens, whether by "protecting" them from globalisation, or by allowing lower taxes on restaurant meals. To nervous neighbours, that sounds less like a plan for Europe than a prescription for selling Europe to French voters.

French officials are perfectly well aware of how they are seen from abroad. In Paris they insist that France will run a "modest" presidency, and act as an honest broker during its six months in the chair of EU ministerial and summit meetings—even on the most divisive dossiers such as Turkey's bid to join the EU (fiercely opposed by Mr Sarkozy, despite the unanimous EU agreement to open membership talks).

But already the strains are showing. The French presidency will be judged a success if it pulls off just one tricky task: turning a set of lofty EU pledges on tackling climate change into concrete measures spelling out exactly how much each country must cut its carbon emissions between now and 2020. On this issue, Europe is divided into two ideological camps: a liberal one, including Britain and the Nordics, who believe in cutting carbon emissions across the globe by as much as possible for the lowest cost; and a more protectionist one that wants to fight climate change but still preserve European jobs in energy-intensive industries. This camp wants to erect barriers to imports from countries that are not making matching sacrifices on carbon emissions. France is not merely a member of this camp, but its leader: Mr Sarkozy says that demanding "reciprocity" on tackling climate change will be a priority of his EU presidency.

Nor is the French president neutral in the divisive debate over the role of the European Central Bank. On the eve of France's EU presidency, Mr Sarkozy argued for the umpteenth time that the bank should seek to promote growth, and not just focus on curbing inflation, adding that the euro was "overvalued" by 30%.

Peter Mandelson, the trade commissioner, is equally correct to complain that he is being "undermined" by Mr Sarkozy in the world trade talks. France is furious that the British commissioner proposes to dismantle trade barriers that shield EU farmers from competition, saying that he has not secured matching concessions from trade partners (even though he is working within an agreed EU mandate). Senior French officials have made clear they will seek to block what they see as a "bad" world trade deal, even though they ought to be neutral in the presidency.

Mr Sarkozy inspires mixed feelings for other reasons, too. Nobody in Brussels doubts that the next six months will be unusually dynamic. With the EU struggling to cope with last month's Irish rejection of the Lisbon treaty, some thoughtful types even welcome Mr Sarkozy's impatience with the "business as usual" reaction of the pro-European establishment, whose grandees argue that Ireland must simply vote again, if need be under threat of expulsion or marginalisation. The EU is "not going at all well," Mr Sarkozy told French television on June 30th, adding that "profound changes" were needed to "the way we build Europe".

The politician in the palace

Many in federalist circles were quick to dismiss Ireland's no voters as ignorant and bamboozled by the lies of anti-Lisbon campaigners. In the Elysée Palace, in contrast, a more respectful analysis is offered. Voters felt that Ireland's national identity was under threat from EU integration, it is suggested. Europe should be more careful about imposing unpopular measures, insists the Elysée. Harmonisation of things like minimum wages or identity cards will simply "screw up Europe" by provoking a backlash. But Mr Sarkozy's sensitivity to voter sentiment cuts both ways. His plan to make Europe loved again, set out this week, is tailored not merely to appeal to French sensitivities, but also to respond to specific gripes of interest groups, from lorry drivers wanting fuel taxes capped to French anchovy fishermen wanting fisheries to be reopened against scientific advice. (There are so many anchovies, you can "walk on the sea" without wetting your feet—"or so I am told", said Mr Sarkozy, carefully giving himself a get-out clause even as he pandered.)

On many of these populist measures, France is isolated. The odds are that other EU countries will not agree to lower taxes on restaurants in the next six months, nor to cap VAT on fuel for lorry drivers. The anchovy fisheries will stay closed, by EU order. So why promise such impossible things? After all, when they fail to happen, French voters will surely blame Europe. It is a tough question for Mr Sarkozy, the EU's new boss, to answer. But if in fact the president is just another French politician who is happy to make Europe the scapegoat whenever it suits his domestic purposes, it is a question hardly worth asking at all.



Housing slump

Collateral damage

Jul 3rd 2008
From The Economist print edition

Getty Images



The latest blows to the property market will pound the economy too

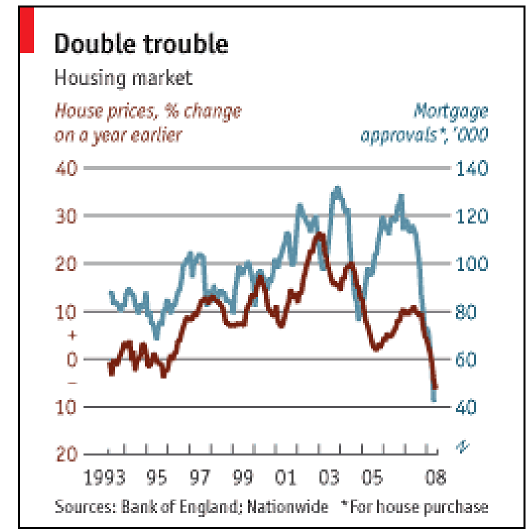
AFTER the longest and biggest boom in post-war history, it is payback time for Britain's ever more troubled housing market. As shares in homebuilders wilt following the failure of Taylor Wimpey, the country's largest, to raise urgently needed capital (see article), there are wider worries that Britain may revisit the trauma of the early 1990s, when a housing bust led to a deep recession. With activity in the services sector at its lowest since October 2001, the economy looks perilously vulnerable to falling housing wealth and the collapse in mortgage finance, residential investment and property transactions.

The mortgage market has already plumbed unprecedented depths. Figures released this week revealed that a mere 42,000 loans had been approved to buy homes in May, well under half the number a year earlier and below even the trough reached in the early 1990s. New approvals are closely watched because they point the way to house-price changes (see chart). The declines that started late last year are continuing apace, according to Nationwide Building Society. House prices fell by 0.9% in June, leaving them 6.3% lower than they were a year earlier.

The outlook for both the mortgage market and house prices is grim. On July 3rd the Bank of England's survey of credit conditions reported that lenders intend to restrict new home loans still more over the next three months. Following the latest statistics on mortgage approvals, Capital Economics, a consultancy, said that it expected house prices to fall by 15% in the 12 months to December 2008. It is forecasting a further 12% decline in the following year.

The interplay between the distressed mortgage and housing markets is likely to get worse as more homeowners find themselves with negative equity (meaning that their homes are worth less than the loans on them). Working out the numbers affected is tricky, says David Miles, an economist at Morgan Stanley, an investment bank, and for many the shortfall may be quite small. With those provisos he reckons that a 15% fall in

house prices could push 1.2m households under water; and a 20% decline might affect 2m, as many as in the dog days of the early 1990s.



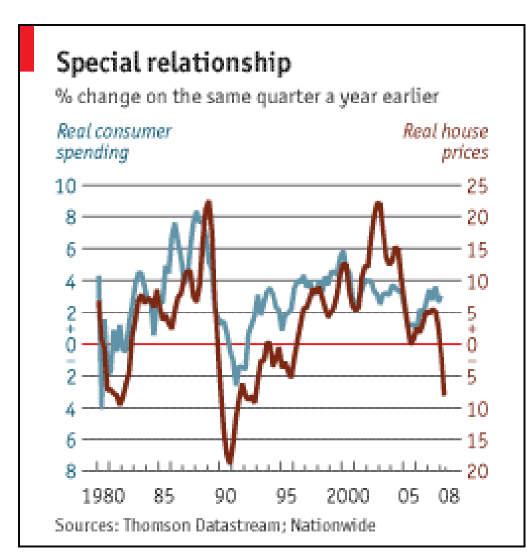
As everyone involved in property, from homeowners, estate agents and lawyers to builders and their workmen, feels the pain, there will be wider effects. There are three main ways in which the housing market's malaise may infect the economy. Each threatens to do considerable harm.

The first channel is through lower residential investment. Housing starts fell by 24% in the first quarter when set against the same period in 2007 and things have got worse since then. Kate Barker, a member of the Bank of England's monetary-policy committee, recently said that the probable decline this year would be on a much bigger scale than in the slump of the early 1990s. The likely fall in investment could slice over a percentage point off GDP growth in both 2008 and 2009, according to Ben Broadbent, an economist at Goldman Sachs, an investment bank.

A second way in which the housing slump will hurt the economy is by slashing the demand for consumer goods linked to property transactions. When people move they typically borrow some extra money to pay for equipment to kit out their new home. That source of demand will take a big knock, since the turnover of homes may fall by 30-40% this year. The effect, estimates Mr Miles, could reduce GDP growth by a further 0.2-0.3%.

The third route is through the decline in property wealth, and this is a matter of considerable controversy. For many years it was taken for granted that there was a strong relationship between house prices and consumer spending (see chart). More recently the Bank of England has cast doubt on the link.

The apparent breakdown in the relationship in the early years of this decade, when consumers did not respond to a surge in house prices by spending more, seemed to support the central bank's view. This year too, shoppers appear unfazed by falling property wealth. Household spending rose by 1.1% in the first quarter of 2008 compared with the last three months of 2007. Official figures for retail-sales growth in May were so buoyant that they aroused incredulity in the City.



But even if the strength of household spending in early 2008 turns out to be genuine, it may prove short-lived. Consumer confidence fell in June to its lowest level since March 1990, according to a survey by GfK NOP, a research outfit. Until this year the former link between house prices and spending appeared to have reasserted itself. In any case, the earlier breakdown noted by the central bank arguably reflected the influence of a long bear stockmarket in curbing consumer spending.

According to Ray Barrell of the National Institute of Economic and Social Research, a 15% decline in house prices over the next two years would reduce the increase in consumer spending by one percentage point a year. The effect on GDP growth would be smaller, bringing it down by about half that amount over the next year, since much of the spending shortfall would leak out into imports. Clearly, the impact would be bigger if house prices fell more steeply.

Putting these estimates together, the potential economic harm is evident. Mr Miles thinks the outlook is better than in the previous housing bust, because borrowers do not face the sort of shock produced in the late 1980s when the Bank of England doubled the base rate in little more than a year. Even so, the credit squeeze is raising effective borrowing costs as banks restore their margins on new and maturing fixed-rate mortgages. With inflation out of its box, the central bank can do little to help, and may indeed have to raise interest rates to show its inflation-fighting resolve. Coming on top of the erosion of consumers' purchasing-power by soaring oil and food prices, the housing slump looks set to inflict some hefty collateral damage.

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WORLD
BRITAIN

Homebuilders

Throwing in the keys

Jul 3rd 2008
From The Economist print edition

When companies need cash and shareholders say no

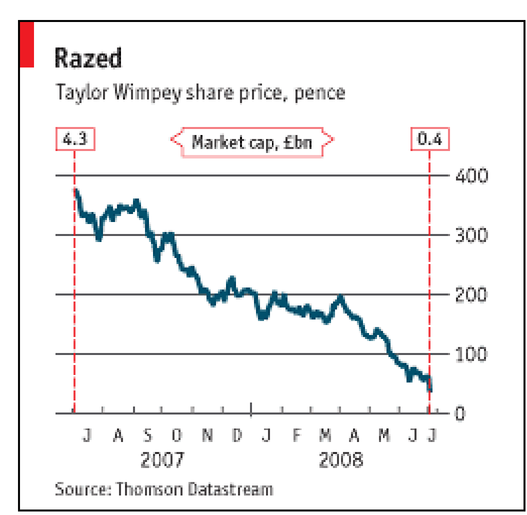
AT THE back of every mortgage lender's mind is the fear that, in a downturn, those whose homes (and other assets) are worth less than their mortgages will simply drop their keys through the letterbox and walk away from their debts. Should banks now start to worry that the companies which built those homes will do likewise? Taylor Wimpey, Britain's biggest homebuilder, went to its shareholders for £500m ($1 billion) to shore up its balance-sheet. It returned on July 2nd without an extra penny to its name. A shudder ran round the stockmarket and Taylor Wimpey's share price, already weak at the knees, gave way.

With house prices collapsing and sales of new homes grinding to a halt, the firm, with net debts of about £1.7 billion and a market value of some £370m, needs extra cash because it risks breaching the conditions on some of its bank loans. Yet in a business where timing is at least as important as location, Taylor Wimpey's capital-raising could hardly have come at a worse moment. For on July 1st, just as it tried to get investors to make final commitments, news emerged that in June house prices had fallen by 6.3% from a year earlier, their biggest drop since the previous housing bust in the early 1990s.

Within hours the builder's potential backers began to steal away. "In the morning there was one big new investor willing to come in for a significant chunk," says a person familiar with the talks. "By lunchtime it had scaled back [the amount it was willing to inject], and in the late afternoon it pulled out."

The next day Taylor Wimpey wrote down the value of about £660m-worth of land on its books (£550m of it in Britain) and said that the British housing market was falling even faster than in the 1990s. Its shares, worth just a twelfth of what they had been a year earlier, all but halved again (see chart), and those of other builders followed them down. It was a day of bad news on various fronts. Marks & Spencer, the retailing bellwether, announced its biggest drop in sales in three years. Even the pound dipped against the euro.

The main lesson from Taylor Wimpey's travails—admittedly an old one, now to be relearned—is that balance sheets that are light on equity and heavy on debt may help bump up earnings when times are good but leave firms ill-equipped in a downturn. The company blithely took out loans while burning cash to keep shareholders happy: last year it handed back £117m in dividends and spent £252m buying back shares (at more than ten times their current price). These sums, were they still on its balance sheet, might just be enough to keep its bankers satisfied.



Another lesson—and this is the one that has really spooked the markets—is that the wider economy will not emerge from the credit crunch unscathed. Having slashed the supply of mortgages by insisting on bigger deposits, banks are now looking hard at their lending to companies, pushing them to reduce borrowing and raise equity. They are also enforcing loan conditions that they might previously have let slide. Taylor Wimpey "is a sign that credit markets have tightened again without equity markets noticing", says Colin McLean, a fund manager at SVM Asset Management. He reckons a large number of firms now need to raise capital, but have yet to share this fact with their owners.

A further worry is that Britain's shareholder-friendly methods of raising capital are breaking down as stockmarkets fall and companies have to rustle up sums that are greater than their market value. The tried-and-tested British rights issue, which entitles all shareholders to buy discounted shares in proportion to their existing holdings and pays underwriters to mop up the unwanted ones, has proved cumbersome.

It is also vulnerable to short-selling when shares are in free fall, as often happens when companies urgently need cash. A variation used by Barclays, a bank, to raise £4.5 billion on June 25th, may have promise: big shareholders agreed in advance to buy large blocks of discounted shares and then pass them on to smaller ones at the same price.

Yet in Taylor Wimpey's case this new approach failed. Big owners were unwilling to back the firm beyond agreeing to buy enough shares to keep intact the proportion of the firm they already owned. They have not quite thrown in the keys, but if the company cannot come up with fresh equity somehow in coming months, they might just as well have done so.

Health-care reform

Keyhole operation

Jul 3rd 2008
From The Economist print edition

Planned surgery for the NHS turns out to be less radical than billed

NO LONG-MARRIED couple could have made more fuss about an approaching diamond anniversary than Britain's government has over the 60th anniversary of the National Health Service on July 5th. The build-up started more than a year ago, when the incoming prime minister, Gordon Brown, decided the electorate could do with a history lesson on this cherished institution (see article). He promised that his Labour Party, which had "created the NHS, that has always invested in the NHS, that has always believed in the NHS", would be the party that renewed it. He commissioned Lord Darzi, a surgeon and health minister, to come up with a new plan in time for the NHS's big day.

What with the publication of an interim report last October and multiple leaks since then, Lord Darzi's final report on June 30th felt anticlimactic. A much-heralded new "constitution" turns out to be a flowery restatement of existing rights, such as the entitlement to choose a hospital or receive any treatment approved by the NHS's spending watchdog. Earlier hints that it might detail patients' responsibilities too—to lose weight or give up smoking before surgery, for example—have yielded nothing. And proposals in the interim report to carpet the land with polyclinics—halfway houses between GP surgeries and district hospitals—have, after some critical reviews, been toned down and relegated to a separate report on primary care.

Instead, there was much talk of a new focus on the quality rather than quantity of care. That is handy: the big budget increases the NHS has got used to in recent years are to stop in these straitened times. It is also a disturbing reminder that care in the NHS now is patchy, with an over-reliance on agency nurses in London and the south-east and frightening rates of hospital-acquired infections in many hospitals.

Lord Darzi thinks more information will help patients choose the best places to get treatment, and prod other institutions to raise their game. From next year, hospitals will put out annual "quality reports", with data on safety and outcomes. Other specialities will have to follow cardiothoracic surgery and fertility treatment in coming up with quality indicators: survival rates for individual heart surgeons have recently begun to be published and the success rates of IVF clinics are released. Patients will be asked how they feel before and after treatment, and how satisfied they were with their care. Around 3-4% of a hospital's budget will depend on the exercise.

It will be difficult to measure health-care outputs—heart surgery and fertility treatment are unusual in having results (survival; pregnancy) that are clear-cut and apparent soon after treatment. And suppliers may cherry-pick easier cases or steer patients towards less-appropriate care in order to look good; this is already a problem in education, where league tables encourage schools to gerrymander their intake and push students towards easier courses. But it is better than boasting indiscriminately about the amount of taxpayers' money "invested" (as Mr Brown has an infuriating habit of doing). And it is the way things are moving elsewhere. America's big insurers and managed-health organisations are increasingly looking at quality indicators when purchasing and paying; and Lord Darzi says common Europe-wide measures are being developed that will make it easier to see which countries closer to home do best.

Britons are hardly the only people to fret about health care, and they pay less for it than most. But in exchange for the security of a largely state-funded system they have a state-run monopoly that is unresponsive to patient needs and slow to innovate. With health-care inflation outstripping the ordinary kind and an increasing aversion to higher taxes, Britons' extraordinarily low level of private spending on health may have to change.

Royalties on art

Sharing the wealth

Jul 3rd 2008
From The Economist print edition

Artists do battle to enrich their heirs

Sotheby's



Mr Hirst gilds his calf

ON THE very day that a study by Francis Bacon, who died in 1992, sold for £17.3m ($34.4m) in Christie's biggest contemporary-art sale, a group of British artists fired the opening salvo in what could prove a drawn-out battle. Should their heirs be entitled to royalties on such sales? Led by Damien Hirst, Britain's most commercially successful artist, more than 500 signed a letter to the *Telegraph* urging the government to give them that right. "Our loved ones often sacrifice a lot to support an artist in the family," the letter went, and it was only fair that they got a share of the profits.

For the past two years 4% of the price of a work by a living artist sold through an auction house or by a dealer has been payable to the artist. Sales of less than €1,000 (£796) are exempt, and the tax is capped for anything worth €500,000 or more. Throughout the European Union the tax is payable on sales of works by living artists or those who have died within 70 years; in Britain it is only works by living artists that qualify. The EU allowed Britain this exemption until 2012. Mr Hirst and his colleagues would like to make sure it is not extended.

The image of the penniless artist starving in his garret makes for great opera but poor commercial logic. The artist's resale right (ARR) benefits a far smaller proportion of artists than its supporters might assume. A study sponsored by the *Antiques Trade Gazette* showed that, in the 18 months to August 2007, 10% of the 1,104 artists benefiting from ARR in Britain (around half of whom are British) got 80% of the pot; the bottom 30% received less than £100 each. The royalty has also proved cumbersome and costly to collect.

Most serious is the effect that the extra cost of buying and selling might have on London as an art market. Collectors and curators flock to it twice a year for the auction season. They visit dealers and meet artists they might not otherwise have come across. But people who sell art at auction in London—and there have been more and more during the current boom—are only too aware that they can sell elsewhere: in New York, for example, Geneva or Hong Kong, where the Chinese contemporary market grew by nearly 1,000% between 2003 and 2006.

Adding to the cost of buying and selling art by extending ARR will ensure that more people receive royalties, but not many more. (The lion's share in France goes to seven families; most of them are very well off, including the Picassos and the Matisses.) It will do little for London as an art-market centre—and still less for the quality of its art.

Scottish politics

A hard pounding for Mr Brown?

Jul 3rd 2008 | GLASGOW
From The Economist print edition

After Wendy Alexander's ouster, Labour faces a by-election from hell

PA



WHEN the 1922 general election swept the Labour Party to dominance in west-central Scotland, a Conservative lamented that it was the worst national disaster since Flodden, a 16th-century battle in which the English crushed the Scots. So recorded the young Gordon Brown in his biography of James Maxton, one of the authors of that Labour victory. Now the prime minister may be facing his own Flodden at a parliamentary by-election in Glasgow East, hitherto one of the safest seats in Labour's Scottish heartlands.

At first sight, it looks improbable. David Marshall, the MP whose resignation has precipitated the contest on July 24th, won 60.7% of the vote and a 13,507 majority at the 2005 parliamentary election, leaving the Scottish National Party (SNP) with just 17% of the vote. Yet these are fraught times for Mr Brown. Labour was beaten into fifth place in the Henley by-election on June 26th. And the Scottish Labour Party is in disarray: Wendy Alexander, its leader, resigned on June 28th, brought down by breaching the rules on political donations.

Glasgow East, a sprawling mess of rundown inner- and outer-city suburbs straddling the M8 and M74 motorways, is classic Labour territory, but dereliction and poverty also make it ripe for plucking by a rival party. Expanses of smart new housing speak of years of expensive regeneration, but boarded-up apartment blocks show there is much more to do. Only 4.5% of the workforce claim unemployment benefit, but around a fifth of working-age adults are officially incapacitated, so the effective unemployment rate is above 25%.

The biggest challenge facing all parties is apathy; since 1997 no election in Glasgow East has seen more than half the voters turn out. "I don't vote," says the owner of a pet-grooming parlour. "They promise miracles and give you nothing."

Labour's best bet is straightforward tribal loyalty. Jimmy Stewart, a retired shipyard worker, says: "Families here have always been Labour, I don't think it will change." Among the young, however, there are signs of disaffection. Patrick McShane and Craig Brown, in their 20s, say they will vote Labour but launch into a tirade about the lack of jobs. "Government folk tell us to get off welfare and into work but they bring over Polish people to take our jobs," complains Mr Brown.

The SNP, which took just under 30% of the vote in the area to Labour's half in the 2007 Scottish Parliament elections, has a solid base. "Vote Labour? You must be kidding. SNP!" snort two middle-aged women. James Hilston says he's switching to the SNP because of the abolition of the 10p tax rate. "I think Gordon Brown has been worse than Thatcher," he says. But running the devolved Scottish government for a year may hurt the SNP. "They've dropped some of their pledges," says Frank Lappin. "Like giving first-time home buyers £2,000 and cutting class sizes."

It points to a hard, gritty campaign, in which Labour will not be helped by a divisive campaign for the Scottish leadership. The two most likely candidates, Iain Gray and Andy Kerr, both former ministers, are similar only in their lack of charisma. Mr Gray is close to Alistair Darling, Britain's chancellor of the exchequer, for whom he worked as a political adviser. Like Messrs Brown and Darling, he is averse to devolving more power to Edinburgh and holding a referendum on independence, both policies that were controversially adopted by Ms Alexander and supported by Mr Kerr.

Should this issue dominate the campaign, the SNP will be entitled to accuse Labour of being both in

disarray and under the thumb of their leaders in London. Labour depends on support in Scotland to keep its Westminster majority healthy—at least for now. On July 1st a Conservative Party committee under Ken Clarke unveiled proposals to reduce the voting rights on English-only laws of Scottish, Welsh, and Northern Irish MPs.

It all makes for an unusually complex by-election. “Labour ought to win this very safe seat, but given that Labour’s poll rating is at an all-time low and the SNP continues popular, you cannot rule out the SNP’s pulling it off,” says John Curtice of Strathclyde University. If that happens, Mr Brown, like James IV of Scotland, may find himself fatally wounded.



Student politics

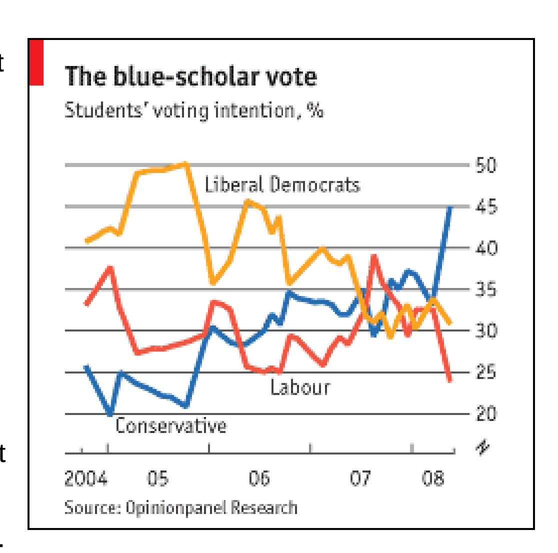
Old heads on young shoulders

Jul 3rd 2008
From The Economist print edition

What do we want? Fiscal prudence, property rights and lower taxes

THE oft-quoted maxim that a man who is not a socialist at 20 has no heart, whereas one who is still a socialist at 40 has no head, has been variously attributed to George Bernard Shaw, Winston Churchill, Woodrow Wilson and Otto von Bismarck, among others. Whatever its origins, the path that leads from the student view of property as theft to an appreciation of low taxes is well-trodden, often suspiciously soon after employment sets in.

Now, it appears, many students are starting adulthood differently. A report published on June 26th by Opinionpanel, a research outfit that specialises in polling students, documents a big shift in political allegiances on campus since 2004 (see chart). In those days the Liberal Democrats were the students' favourite; support for the Tories hovered between a fifth and a quarter, and a third supported Labour. Now fewer than a quarter support Labour, and the Conservatives have soared to 45%.



One reason for these shifting allegiances is the race to the centre ground: it is much harder to fire young minds with technocratic reform of knackered old public services than with free love and a new world order. Another is Labour's decade of electoral domination. For today's young rebels in search of a cause, the Left is the establishment: an 18-year-old starting university this autumn will have been just seven when Labour came to power. Then there is the advent of university fees, and the resulting debt: students who will have to pay back perhaps £20,000 towards their studies are more interested in getting a good degree and a decent job afterwards. And they know that accountancy and law firms would rather youngsters spent their time on essay-writing and internships than on marches and sit-ins.

This is surely excellent news for the Tories, particularly their youngish, newish leader, David Cameron. A big jump in the number of students saying they would vote for his party straight after his barnstorming leadership bid at his party's conference in October 2005 suggests that he personally is attracting new young voters. The fall in support for the Liberal Democrats will be welcomed too: Britain's third party has had a nasty tendency to split the vote in Tory target seats and has long been particularly popular with students, perhaps because of its status as a plucky political outsider, or its line on student fees (against) and legalising cannabis (for).

As well as changing today's political landscape, this shift will have consequences in future years—albeit ones that are hard to predict. If these hard-headed youngsters shift rightward as they age, the nursing homes of the future could be filled with wild-eyed disciples of Ayn Rand and Milton Friedman. Or perhaps the pattern will be reversed, and three decades from now, middle-aged actuaries will belatedly come to appreciate Trotsky and the labour theory of value.

David Davis

The free vote

Jul 3rd 2008
From The Economist print edition

PA



Davis takes on the sceptics

A single-issue by-election hits rural Yorkshire

THE exigencies of the war on terror seem a long way from Haltemprice and Howden, one of the more bucolic parliamentary constituencies. There are few obvious targets to strike in this collection of Yorkshire villages, nor much scope for a clash of cultures (the non-white population is under 2%). Islamist recruiters hoping to exploit deprivation should also look elsewhere: five years ago the private-wealth division of Barclays, a bank, rated it the tenth-richest place in the country, once living costs were taken into account.

Yet thanks to its MP, David Davis, the seat has become a forum for the vexed debate on the trade-off between liberty and security that has gripped Westminster. On June 12th, the day after Parliament voted to extend maximum detention without charge for terrorist suspects from 28 to 42 days, Mr Davis resigned as the Conservative home-affairs spokesman and announced that he would quit his seat. He said he would campaign in the resulting by-election, which takes place on July 10th, on the issue of defending civil liberties from 42 days, identity cards, CCTV cameras, DNA databases and other incursions.

It was a quixotic gesture—for Mr Davis's party had backed his desire to oppose 42 days, after all—but those hoping for his campaign to flop completely are being disappointed. True, neither Labour nor the Liberal Democrats have put up candidates, so Mr Davis (whose rivals include a member of the Church of the Militant Elvis Party) cannot claim much of a mandate for civil libertarianism if, as expected, he wins. But his resignation has prompted a response from the government: Gordon Brown, the prime minister, gave a speech on liberty and security five days afterwards, and has more recently exchanged tetchy letters with Mr Davis.

As for the Tories, some senior figures deplored Mr Davis's "self indulgence" and fretted that the loss of one of their big-hitters would create the party's first bad-news story for months. The party has suffered no dip in the polls, however. Others speculate that Mr Davis is trying to undermine David Cameron (who defeated him for the Tory leadership in 2005), and could be a thorn in his side from the backbenches. But the candidate has ruled out ever leading his party; Mr Cameron campaigned for him on July 2nd and may yet bring him back into the shadow cabinet.

There is, however, a criticism that is harder for Mr Davis to rebut—that he would have served the liberal cause better by sticking around to be home secretary in the next Tory government. Repealing 42 days, to which the Tories (with a caveat or two) are committed, would be an obvious early move. He insists graciously that this could be done just as well by Dominic Grieve, his replacement, but some doubt that. Civil liberties is a tricky issue for the Conservatives, who have both a libertarian wing and an authoritarian one. On the "Nixon in China" principle, Mr Davis's background (he grew up on a council estate and is no bleeding heart on crime) gives him the cover to take an enlightened line on civil liberties; Mr Grieve, a privately-schooled QC, lacks this advantage.

Instead, Mr Davis envisages his role after the by-election as that of one-man pressure group. Public opinion can seem an insurmountable barrier for civil libertarians (there was a clear majority in favour of 42 days). But Mr Davis notes that popular support for ID cards has slipped as voters have been made aware of their drawbacks. “Maybe something similar can be achieved on detention without charge,” he says, brandishing letters of support from the likes of Tim Collins, once an army colonel, and Terry Waite, a former hostage.

If Mr Davis sounds as if he is in this for the long haul, it is because he fears that the threat to Britain’s liberties comes from gradual erosion over time rather than a frenzied assault by a particular government. “Drop a frog into boiling water and it will jump straight out,” says Mr Davis. “Put it into lukewarm water, slowly turn up the heat, and it will die.”

Bagehot

The shock of the old

Jul 3rd 2008
From The Economist print edition

Illustration by Steve O'Brien



The National Health Service has lasted long enough to look modern again

NOT long ago, Bagehot had a baby. Miss Bagehot came into the world in a National Health Service (NHS) hospital in London, attended by an Azeri midwife, a Kenyan anaesthetist, a Moroccan nurse and an Iraqi paediatrician. The patients were almost as varied as the staff: the new mothers ranged from raucous Cockneys to Anglo-Indian Brahmins. It was a bit shoestring and chaotic, with a faint air of Blitz-spirit stoicism; but, in its essentials, the service was impressive. It was a classic NHS experience.

A dream of post-war collectivism, the universal, tax-funded NHS was launched on July 5th, 1948. In the 60 years since then it has intermittently seemed inadequate, hopelessly antiquated and plain doomed. But it is now looking oddly contemporary—partly because it has survived long enough for its principles to be relevant once more, like a retro fashion that suddenly seems cool again, and partly because it has evolved. Two of the four big problems that have long beset it are almost solved.

One of those (believe it or not) is the conundrum of how to pay for health care. The basic assumption made in 1948—that demand would decline as the nation's health improved—turned out to be utterly mistaken. Instead, the richer people became, the more health care they wanted. Experts soon worried that the threefold pressures of rising life expectancy, expensive new technologies and spiralling expectations might sink the NHS; patients now lust for perfection and immortality, and find exotic ways to achieve them on the internet.

It seems crazily optimistic to hope that a tax-funded health system can meet these demands—but probably less crazy than relying on other systems. At the last count, America spent 15.3% of its national wealth on health, compared with Britain's total of 8.4%, but many Americans are uninsured. France's system of social insurance is stretched. Moreover, in the future, state-financed universal health care could offer the best way to deal with the consequences of genetic testing, which will be able to identify people's susceptibility to diseases more precisely. Better-off patients should be allowed to pay for extra services that the NHS can't afford, while staying inside the system (a reform that is currently being pondered by a government review); otherwise, the middle classes will opt out, and the sort of social solidarity on view in the Bagehot family's maternity ward will crumble. But the debates that once raged about switching to a different model have abated: the principle of tax funding for most services seems entrenched. David Cameron's Conservatives accept it.

The second almost-solved problem stemmed from a resilient confusion: a peculiar British belief that,

because the state funded the NHS, it should also run all the hospitals. The charge of “privatising the NHS” (roughly equivalent to slaying the first-born) was for decades enough to quash any bid to take on the monolith. That is, until recently. Panicked by nasty headlines, Tony Blair at first simply threw money at the NHS: in real terms health funding has doubled in ten years. But eventually his government, more than any Tory one ever dared, set about introducing choice for patients and competition among hospitals. Whoever is in power, in the long term the NHS is probably on the way to becoming a state-funded market rather than a creaking monopoly.

That leaves two main outstanding glitches. One of them is politics (notwithstanding Mr Blair’s epiphany). The NHS is not only paid for by the state and still overwhelmingly delivered in state-run hospitals: it is overseen by politicians in Whitehall too. This has made it vulnerable to incessant, pointless micro-reforms and distorting central targets. State control also skews priorities. In particular, preventive measures, which can seem unpopularly nannyish and win few votes, have been neglected (though Gordon Brown has emphasised check-ups and the like). That will matter more as the costs of obesity and other “lifestyle” diseases bite. There is periodic talk of making the NHS independent; but the amount of cash it consumes means politicians will always be held responsible, and probably do some myopic meddling.

The other obstacle is the doctors. Nye Bevan, one of the NHS’s architects, famously remarked that to sign up the doctors he “stuffed their mouths with gold”. The current government has followed his precept, awarding them lavish raises while, in some cases, allowing them to do less work—which helps to explain why the cash bonanza has not yielded a commensurate boost in output. The powerful medical unions have sometimes resisted sensible ideas, cunningly persuading patients that their own interests and the doctors’ coincide—another unhelpful confusion.

Better than billed

The griping of staff helps to explain why some people who are happy with their own care nevertheless think that the service as a whole is failing. Yet for all the noise, satisfaction with the NHS, according to some pollsters, is high and rising. Once the nation’s political priority, health as an issue is less salient than it has been in 20 years. And though the NHS’s imperial size—in England it has well over 1m employees—makes generalisations perilous, on balance the polls reflect an underlying improvement. Too many people still pick up infections on dirty wards, or have their operations cancelled at the last minute. But there are more nurses and doctors (around a third of them foreign, like baby Bagehot’s); and on average people are waiting less long for treatments than they once did, and being cured of the worst diseases more often.

Britons are an incoherent lot. Convinced of their Anglo-Saxon tight-fistedness, left-wing politicians have felt obliged to moderate or camouflage their egalitarian urges. Free-marketeers, meanwhile, moan that the British are at bottom soggy socialists. Both are right: British voters are willing to tolerate greater inequalities than many Europeans, but are stubbornly attached to a few totems of communitarianism. In the case of the NHS, for all its shortcomings, they may have turned out to be right.




Conflict resolution

The discreet charms of the international go-between

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From The Economist print edition

Illustration by Claudio Munoz



A murky world of back-channels, secret meetings and close encounters for a new breed of problem-solver, both secular and (see article) religious

FOR two months, Kenya, East Africa's most prosperous and supposedly stable country, hovered on the brink of self-immolation as two warring political factions ripped the country apart after a disputed election at the end of 2007. Kofi Annan, the former secretary-general of the United Nations, was brought in to try to resolve the conflict between the ruling party, which was accused of rigging its presidential victory, and the opposition Orange Democratic Movement (ODM). As ethnic violence raged nearby, negotiators from the two sides would sometimes almost come to blows themselves as Mr Annan tried to find common ground between them.

But when deadlock loomed, both sides' negotiating teams were smuggled off to a secret location in a game park for two days, with just Mr Annan and his secretariat, including a team from a little-known group called the Centre for Humanitarian Dialogue (CHD). There, with no distractions from the media and far from the political circus in the capital, Nairobi, came the vital breakthrough. The main outlines of a deal between the two sides were talked through in an atmosphere of relative calm; a new national unity government, comprising both the ruling party and the ODM, was inaugurated a few weeks later.

Originally, Mr Annan had flown into Nairobi with just two people from the CHD, a Swiss-based organisation of mediators. During his six weeks or so of mediating he drew on the considerable resources of the UN, but he also made constant use of his CHD backup.

They provided him with tactical advice on the mediation process, such as when to take the negotiators on "retreat" and how to involve the media. And they also drafted agreements as the two sides spoke during the negotiations, so that at the end of a day an agreed statement could be issued immediately to the press. This gave the mediation the vital momentum that Mr Annan wanted.

The Kenyan talks provide a good example of the sort of skills that a new kind of international mediator can bring to the age-old work of conflict resolution. For as the nature of the world's conflicts has changed in the past decade or so, so the demand for a new type of mediator has grown too.

The CHD, for instance, founded by just four people only nine years ago, now has a staff of over 70. The UN has traditionally provided a forum for the discussion and resolution of international disputes. However as Kreddha, a Dutch-based mediation group, argues: "There are no equivalent mechanisms for intrastate dispute resolution...despite the fact that most violent conflicts today are not international but intrastate

in character.” The new mediators provide the new mechanisms.

Many of these contemporary conflicts involve insurgents, secessionists or even “resource-warriors”, like those in the oil-rich Niger Delta of Nigeria, who clash with governments. Rival politicians can be brought into open conflict by elections, such as in Kenya, or now Zimbabwe.

The new kinds of disputes involve non-traditional parties such as international mining or oil companies pitched against indigenous people, as well as national governments tackling more established terrorist groups. One study has shown that over the past 15 years military victories have resolved only 7.5% of conflicts, while negotiations have prevailed in 92% of cases; “the challenge is thus not being a skilful warrior but a skilful negotiator.”

The UN might, at best, offer some bureaucratic and political clout, but it is also big, cumbersome and leaky. In its place, the new mediators operate on a much smaller scale and offer discretion, secrecy and flexibility. Mr Annan used the CHD in Kenya because it has no political agenda, so could be relied upon not to leak material in order to influence the talks one way or another. These mediators are ideal for getting involved in highly charged disputes between governments, for instance, and indigenous “terrorist” groups; they can set up back-channels, of the sort that proved vital in bringing about the eventual peace deal between the British government and the Irish Republican Army.

Thus the CHD provided a first conduit between the rebel Free Aceh Movement and the Indonesian government, as the Indonesians refused to use the UN because of anger over its role in East Timor. In Nepal, the CHD established the first links between the government and the Maoist insurgents in 2000. Here a key factor was “plausible deniability”, as was trust. Andrew Marshall, who sought out the first Maoist interlocutors, says that “neither side wanted their own people and cadres to know they were talking to the other side”, so the leaders of both the government and the rebels invested their trust in the third party, CHD, to keep the talks secret. Eventually, several countries got involved and this year the Maoists prevailed in elections.

The CHD also acted as a back-channel between the Spanish government and the Basque separatist movement ETA leading up to a ceasefire in 2006; it is currently trying to bring together the Darfur rebel groups in Sudan as one negotiating body. Kreddha has been involved in mediation work in the Niger Delta, and in New Caledonia between a mining corporation, Goro Nickel, and an indigenous environmental organisation called Rheebu Nuu. Such disputes are often called “resource conflicts”, and require specialist mediators with a knowledge of international law. Another new organisation called Conflicts Forum, founded by a former British intelligence officer, Alastair Crooke, attempts to serve as an interlocutor between militant Islamist groups, such as Hamas and Hizbullah, and the West.

Some mediation work can be instantly glamorous and hugely fulfilling, as in Kenya, but most of it is attritional; often it is pretty boring. Negotiations can drag on for years, but here again the small mediators can add a lot of value. Foreign politicians from America and Britain, for example, may bring a lot of pressure to bear on a dispute for a short amount of time, but inevitably they come and go according to the whims and demands of domestic politics. Professional mediators can stick with a conflict for years, thus building up a level of trust and knowledge that cannot easily be replicated. Much of a mediator’s work lies in getting the logistics right; trusted third-party interlocutors are needed simply to arrange meetings and book hotel rooms which will not be bugged by the other side.

In the case of CHD, it can also get visas and facilitate travel for “terrorists” taking part in talks in neutral venues like Switzerland or Norway. Both are strong financial backers of the centre, and neither is a member of the EU; they are thus outside the conventions restricting travel for those on some terrorist watch lists. Small countries backing small mediators can make a big difference; the betting now is on Mr Annan and his team trying to repeat their Kenya trick in beleaguered Zimbabwe.

Mediation and faith

Not a sword, but peace

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From The Economist print edition

In some cases, only the religious have the patience to be reconcilers

WHEN George Bush visited Rome last year, he wanted to see everybody who mattered in world affairs: Pope Benedict, the leaders of Italy—and members of the Sant'Egidio community.

AFP



Tumbling barriers: George Carey and Yasser Arafat

Started by a high-school student in 1968, this Roman Catholic fellowship now has 60,000 members in 70 countries. Its founding ideals were prayer, mission and solidarity with the poor. But it has also become the leading player in a crowded sector, that of faith-based peacemaking.

Helping warring parties (who may or may not profess a religion) to come together is not quite the same as inter-faith dialogue, though the two things can overlap. Faith-based mediation often involves putting to work in hard secular places the virtues that at least some religious people possess (discretion, modesty, empathy, a non-judgmental cast of mind, an ability to overcome cultural barriers).

Since the early 1990s, Sant'Egidio mediators have helped broker deals in places like Mozambique, Guatemala, Kosovo and, most recently, Côte d'Ivoire. Africa and Latin America are the main fields that Christian peacemakers plough. What many world leaders want to know is whether such groups bring anything unique to the business of reconciliation.

According to Mario Giro, Sant'Egidio's head of international affairs: "What really makes the difference is neutrality, impartiality…and the ability to bring in outside powers as guarantors of an eventual deal." He feels faith-based bodies know more about the grassroots reality of a situation because of their contacts with local religious figures, be they priests, imams or missionaries. "And all the more so if they are involved in inter-religious dialogue."

Sant'Egidio's mediators are not the only faith-based go-betweens to have done well. Vatican diplomats have mediated between governments and rebels in several African nations, notably Burundi, where the Holy See's man, Michael Courtney, was killed in 2003 at a time when he was deeply involved in peace work.

The Netherlands Institute of International Relations found 27 Christian, Muslim and multi-faith peace groups to look at for a study issued in 2005. Their strengths, it reported, included "long-term commitment, long-term presence on the ground, moral and spiritual authority, and a niche to mobilise others for peace". But there were weaknesses, such as "a lack of focus on results and a possible lack of professionalism". A further risk, the institute said, was that the impulse to proselytise would obstruct the

search for peace.

Peacemaking by Christian evangelicals in south Sudan seems to have been mired at times by an unhappy mix of missionary work and mediation. That is a qualification to the view, set out in a 2001 report from the Congressionally-funded United States Institute of Peace, that “faith-based organisations have a special role to play in zones of religious conflict.” In the Middle East, any progress has stemmed from secular initiatives. But that, says Sharon Rosen, could be a reason why progress is so scant.

The trick in all peacemaking is to find new commonalities, says Ms Rosen, an adviser to Search for Common Ground, a non-government body dedicated to conflict resolution and prevention. Its Jerusalem offices will soon host the secretariat of a Council of Religious Institutions of the Holy Land, set up last year: members include the Chief Rabbinate of Israel, representatives of the *sharia* court of Palestine and the Christian patriarchates. One aim is to build mutual respect in a way that will assist more conventional peacemaking by diplomats and politicians. “I do not believe that inter-faith dialogue will bring about peace in the Middle East,” says Ms Rosen. “But I do believe that it is essential if peace is to be brought about. To ignore religion is a very grave mistake and I think the Oslo accords made that mistake.”

Her husband, Rabbi David Rosen, co-signed an ambitious effort to correct that error: the Alexandria declaration of January 2002, in which rabbis, muftis and top Christians, including George Carey, then Archbishop of Canterbury, agreed that the “holy land” was too sacred to be sullied by blood. Perhaps the best thing about such idealistic initiatives is that they create human networks of trust that come into play (often secretly) in crises—such as the siege of Bethlehem’s Church of the Nativity in May 2002. The right sort of religious peace-broking is really vital if the dispute itself has to do with religion.

America’s carmakers

That shrinking feeling

Jul 3rd 2008 | DETROIT AND LONDON
From The Economist print edition

High petrol prices land Detroit’s Big Three in even deeper trouble

THIS week shares in General Motors (GM), America’s biggest carmaker, fell below $10, valuing the giant firm at little more than $5.6 billion. The last time GM’s share price was this low, the Cadillac Eldorado had yet to grow fins and Volkswagen’s Beetle was a funny-looking novelty on American roads. That was in 1954.

Things are just as gloomy elsewhere in Detroit. Ford has abandoned all hope of returning to profit, as promised, in 2009 and appears to be bracing itself for a loss in 2008 even bigger than last year’s $2.7 billion. And on June 26th Chrysler was led to deny rumours that it was preparing to file for bankruptcy, after drawing down a $2 billion credit line from its owners, Cerberus Capital Management, a private-equity firm (see article), and Daimler.

It was not meant to be like this. At the beginning of the year both Ford and GM were expecting the credit crisis to knock sales in the first half, but they were still cautiously optimistic that they would soon reap the rewards of their expensive and painful turnarounds. Along with Chrysler, they had just secured a big package of concessions from the carworkers’ union that went a long way to closing the cost gap with the “transplants”—the lean, non-union factories operated in North America by their Asian and European rivals.

Independent reports by J.D. Power and Harbour showed that Detroit was also fast catching up with the Japanese on quality and productivity. GM’s new Chevrolet Malibu, declared North American Car of the Year in January, was seen as the first domestic product in years to give Toyota and Honda a run for their money in the fierce market for mid-size saloons.

But the carmakers have been ambushed by the disastrous housing market and, above all, by the soaring cost of fuel. Falling house prices have persuaded many people to put off buying a new car, and petrol at over $4 a gallon is radically changing demand. Detroit is still stuck with model ranges heavily biased towards the big, thirsty sport-utility vehicles (SUVs) and pickup trucks that raked in the profits when petrol cost half of today’s price.

The Big Three were certain that America’s love affair with go-anywhere, do-anything, gas-guzzling trucks would never end—so much so that both Ford and Chrysler pinned their hopes of recovery on new versions of their bestselling pickups, the F-150 and Dodge Ram respectively. Chrysler even unveiled the new version of the Ram with a cattle-drive through the streets of Detroit in January (pictured).

AFP



But that conviction has lately been shattered. Figures released this week show that sales of cars and light trucks in America in June fell by 18% compared with the same period a year earlier. Chrysler's sales were down by a stunning 36%, pushing its market share below 10% for the first time in decades. Ford dropped by 28%. Despite flinging costly rebates at the market, GM's sales were still down by 18%. Even Toyota, which was widely expected to overtake GM for the first time last month, took a 21% hit, as it struggled both to sell its big Tundra pickup and to keep up with demand for its popular fuel-sipping hybrids. Honda, by contrast, which unlike Toyota and Nissan has never offered Americans chunky pickup trucks, actually increased its sales by 1.1% thanks to a 26% rise in sales of its economical passenger cars.

Unless there is sudden reversal in the price of oil, Japanese and South Korean brands will make big gains in market share both this year and next. Their North American factories are more flexible than Detroit's are and there is capacity to be tapped back home. Although GM and Ford make some fuel-efficient cars, such as the Chevrolet Cobalt and the Ford Focus, dealers complain that supply is limited and that customers tend to opt for Japanese or South Korean brands when trading down.

GM, Ford and Chrysler are each reacting to the crisis in different ways, but with the same aims—to reduce the speed at which they are burning cash, and to accelerate the arrival of more fuel-efficient models. Ford is slashing its salaried workforce, delaying the launch of the new F-150 by two months because dealers cannot shift the outgoing model, and converting an F-series plant in Mexico to build the relatively tiny new Fiesta, which Europeans will get this summer—more than a year before American buyers.

GM has gone further, closing four truck and SUV factories and putting its Hummer brand up for sale. Analysts reckon GM's $20 billion cash pile is being depleted at a rate of $1 billion a month, making it a near-certainty that it will have to tap shareholders for new funds before long. And this week Chrysler said it would slash production of the Dodge Ram and shut one of its two North American minivan factories. Chrysler's minivans have long been regarded as the firm's "crown jewels", but sales this year have suddenly slowed.

So just how bad are things for the Big Three? Their survival has been in doubt before. But two things are different this time. The first is that the carmakers' finance arms used to bring in cash even in hard times. That is not happening now. More buyers are defaulting on their car loans, and the resale value of SUVs and pickups has collapsed so catastrophically (see chart) that the finance offshoots are losing huge sums on vehicles returned after lease.

The second change is that it seems increasingly unlikely that consumers will eventually shrug off the high price of fuel and return to their old buying habits, which means that Detroit's old business model is now obsolete. Jim Farley, Ford's head of global marketing, describes the market as crossing a "watershed". The problem is that the smaller, more efficient cars that buyers now want, and which will come on stream in a year or two, are far less profitable for both manufacturers and dealers. Denny Fitzpatrick, a GM dealer in California, observes that he makes more money

selling ten Chevy Tahoes (a bloated SUV made by GM) than he does selling 50 Honda Civics (a compact car).

GM and Ford can at least take some comfort from their well-run foreign operations, which are benefiting from growing demand in China, Russia and Brazil. But Chrysler has no such cushion. Worse, it is planning to replace only half its fleet in the four years after the 2009 model year (compared with Honda's 72% replacement and Nissan's 80%). John Murphy of Merrill Lynch believes this is "an active decision by the new owners to rationalise the product portfolio in advance of a break-up or sale". It may not be long before the Big Three become the Not-So-Big Two.



TNK-BP

At war with itself

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The row over the future of BP's Russian joint venture deepens

JUST who is in charge of TNK-BP, a Russian oil firm in which BP, a British oil giant, and AAR, a Russian consortium, own equal shares? The firm's attempt to renew visas for its foreign staff has shown how uncertain the answer is. At a hearing on the subject in Moscow last week, two different delegations showed up, both claiming to represent TNK-BP. Tim Summers, the firm's chief operating officer, who is a former BP employee, said the firm would need visas for 150 foreign workers. But his request was contradicted by Viktor Vekselberg, a TNK-BP director and one of the three tycoons who own AAR. He said 71 visas would be plenty. Mr Vekselberg prevailed, forcing some of TNK-BP's employees to leave Russia almost immediately, and dramatically escalating the row between BP and its partners.

The foreign staff's troubles began, BP says, when an employee who is also a shareholder of AAR deliberately applied for the wrong number of visas. TNK-BP's chief executive, Bob Dudley, a former employee of BP, has since tried to rein in employees close to AAR, but has not been able to because of the divisions at the top. As things stand, some 45 of the firm's employees will now have to leave for good. And this is not the only dispute involving TNK-BP's workforce. Another 150 consultants, seconded to the firm from BP, are unable to work, owing to a lawsuit brought by a minority shareholder who reckons that the fees they charge are a rip-off.

Both sides readily agree that these disruptions will harm the firm, not just by leaving it short-staffed, but also by distracting managers and sapping morale. But neither seems prepared to give in. Stan Polovets, AAR's boss, says that BP is running TNK-BP for its own benefit; he is determined to install more neutral management. BP retorts that the management is perfectly neutral, and that AAR is the one trying to exert undue influence.

In addition to the vexed question of who should be in charge at TNK-BP, the two sides also seem to have some genuine differences over how it should be run. BP, for example, is keen for the company to hunt for more reserves of oil and gas, to make up for BP's own less impressive record in finding oil. The Russian shareholders, however, are more concerned with immediate financial returns. The firm's by-laws seem to give BP the upper hand: it has the right to nominate the chief executive. But as the visa troubles show, the Russian partners have plenty of other ways to assert themselves. On July 2nd they called for an emergency board meeting to secure Mr Dudley's dismissal.

AAR has also filed a lawsuit against BP in Moscow and says it is preparing an arbitration claim against it in Stockholm. Mr Polovets has a list of a dozen more lawsuits AAR might embark on if BP does not come round. BP, meanwhile, insists it has done nothing wrong, and that any unbiased court will find in its favour.

Ultimately, however, most observers believe the row will be settled in the Kremlin rather than in the courts. The problem is that no one knows what Russia's political leaders want. Will the state demand a stake in the firm—and if so, which side will be forced to sell, and at what price? Only one thing seems certain: the longer the authorities take to make up their minds, the less valuable TNK-BP will be.

Starbucks

Grounds zero

Jul 3rd 2008 | NEW YORK
From The Economist print edition

The troubled company wakes up and smells the coffee

FOR years it seemed that American consumers' demand for liquid fuel was price inelastic—whether it was to drive their cars or get their brains going in the morning. Yet $4 seems to have been the price at which demand becomes elastic, for both petrol and a frothy latte. As a result, baristas at Starbucks coffee shops around America are starting to get a taste of what it feels like to be a carworker in Detroit. On July 1st the coffee retailer, based in Seattle, said it would close a further 500 stores in America (in addition to the 100 closures it announced earlier this year), and reduce its workforce of roughly 172,000 by around 7%.

A remarkable 70% of the stores due to close were opened after 2005, which seems to confirm the comment made by Howard Schultz, when he returned to the helm of the company in January, that most of Starbucks' wounds were self-inflicted. As it expanded at a breakneck pace, the company opened too many Starbucks in subprime locations. But the deteriorating American economy is doing further damage. As a premium-priced supplier, Starbucks is suffering from the same trading down that is sending shoppers rushing from Target to Wal-Mart. McDonald's, it seems, has perfectly timed its decision to start selling coffee that is pleasant to drink.

Shares in Starbucks are now trading at barely one-third of their peak value from two years ago. Yet, rather than being a sign of panic, the closures may be evidence that Mr Schultz means to return the company to its focus on quality, rather than growth. After closing all its American stores simultaneously for a brief retraining session a few months ago, there are plans for further improvements in the staff's competence and demeanour, and in the cleanliness and comfort of its shops.

There are also innovations in the works, ranging from healthy smoothies, to a mysterious (and so far unnamed) Italian drink, to further automation. In March Starbucks bought the Coffee Equipment Company, a small outfit that produces a hugely expensive coffee-making machine called the Clover. It is now testing the machines in a handful of its American shops.

Admittedly, there have been some complaints about the introduction of the milder "Pike Place" filter-coffee blend. But on the firm's popular new customer website, MyStarbucksIdea.com, the main concerns are about the quality of the food sold by Starbucks and, above all, its prices. Encouragingly for Mr Schultz, there are also many positive suggestions, from serving vegan food to introducing a loyalty card, which suggests that plenty of customers still care for Starbucks enough to give him a chance to win them back—recession or no recession.

Gambling in Macau

Playing a poor hand

Jul 3rd 2008 | MACAU
From The Economist print edition

An Asian godfather reshuffles

AFP



All that glitters…

AFTER several false starts Stanley Ho, Macau's erstwhile casino monopolist, at last broke through a logjam of litigation and scepticism this week and took his ailing gambling franchise public, agreeing on July 2nd to sell a 25% stake for some $500m. SJM Holdings, as his company is now known, owns 19 of Macau's 29 casinos and has the biggest market share, but its lead is tenuous and the deal was not an easy sell. Hong Kong's new-issuance market is weak after many disastrous offerings this year, and for what Mr Ho wanted to sell—some shabby casinos built to serve what used to be a captive market—it is weaker still.

In 2004 SJM had revenues of HK$34 billion ($4.4 billion), 85% of the total for Macau's gambling industry. Three years later Macau's gambling revenues have doubled, but SJM's have declined. New figures suggest that it may soon lose its leadership to Las Vegas Sands, which owns two giant casinos, the Sands and the Venetian, that are as glittering as SJM's are grim.

A year ago, when a listing of SJM was first being broached, SJM might have expected to be valued at 14 times cashflow, rather than today's seven times, says Billy Ng, a securities analyst at JPMorgan. Back then the Hong Kong market for public offerings was euphoric and the full impact of the entry of two rival firms from Las Vegas, Wynn and Sands, was not so apparent. Efforts to seize that opportunity, however, were delayed by a deluge of litigation by Mr Ho's sister, Winnie, who has long feuded with him over the management of the family's various casino operations. The legal fight postponed a planned listing in January. To allow the deal to proceed this week, investors have been indemnified against any related legal costs.

The offering document was littered with titbits about Mr Ho's empire. He turns out to have an interest in a casino in North Korea; stakes in five of SJM's largest suppliers, including the ferries that bring punters to Macau; and interests in local horse- and dog-racing franchises, a Chinese lottery and various hotels and property.

Disclosing all this information cannot have been easy for Mr Ho. For years he has trod a difficult line, being one of Hong Kong's most visible personalities and appearing at society events, while also running a complicated, mysterious business empire. Why, given the weak market, has he chosen to bring it all to light now?

Perhaps it is the first step in a more profound rehabilitation of SJM, prompted by Mr Ho's acceptance of just how badly it has been gored by foreign competitors. In February 2007 SJM responded with its own elaborate casino across from his old flagship, the Casino Lisboa. But the new Grand Lisboa (pictured above) is far from packed and still lacks an occupancy licence for the hotel above the gaming floor. A

public listing now may not bring in much money, but it provides a way to raise money in future and grant ownership stakes to more competent managers. Mr Ho must have realised that the game has changed.

Economist.com BUSINESS

Opera companies

Music for the masses

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From The Economist print edition

New York's Metropolitan Opera has pioneered a new model

"WHEN I took over, the Met was on a declining slope toward extermination," says Peter Gelb, who took charge as general manager of the Metropolitan Opera in New York City in August 2006. Attendance figures were falling and patronage was dwindling, even as running costs and competition for the cultural dollar were on the rise. But perhaps the biggest problem of all was the product itself: opera has an eminently elitist image. And the 125-year-old Met was the stuffiest of the musical temples for the rich.

Mr Gelb, a former president of Sony's classical-recording division, decided on radical action. With a beefed-up marketing team he launched an outreach programme to attract a bigger and younger audience. (The average age of Met goers is about 65.) He opened dress rehearsals to the public, broadcast opening nights to the plaza at Lincoln Centre and in Times Square, and sold heavily discounted seats for weekday performances. He also increased the number of new productions in the season from three or four to six or seven, and recruited directors, such as Anthony Minghella, who are known to a wide public. But his most revolutionary and most controversial move was the decision to offer cinemas across the world high-definition telecasts of the Met's live performances.

These "simulcasts" made a big splash. During the 2007-08 season over 600 cinemas in America, Australia, Europe and Japan showed the Met's live broadcasts. More than 920,000 people in 23 countries watched eight operas, roughly a threefold increase over the previous season, and about 70,000 more than the total audience of the Met proper during that season. For the next season 11 operas will be televised at an even greater number of cinemas.

The Met's simulcasts are expensive, costing about $1.1m each. They need a production team of about 60; some 15 cameras film the action on stage, backstage and in front of the stage. In its most recent season the Met, which gets 50% of the box-office revenue from simulcast tickets (sold at an average price of $22), more or less broke even with the scheme. This season it expects to make a profit.

But the simulcasts' main point is to broaden the audience. According to a recent survey by Shugoll Research, a pollster, more than 92% of the people who saw one of the Met's performances in a cinema said they were likely to go to a performance at the Met or another opera house. As almost one in five of those surveyed said that they had not gone to the opera in the past two years, and around 5% said they had never been to the opera at all, the Met can justifiably claim that simulcasts are rejuvenating and expanding the audience for opera.

Other opera companies are copying, or planning to copy, the Met's cinematic venture. San Francisco Opera broadcast the first of six (pre-recorded) opera productions in March, proudly proclaiming that it is the first to use "Hollywood feature film-quality digital-cinema format". Tony Hall, boss of the Royal Opera House (ROH) in London, is jumping on the bandwagon, with last year's acquisition of Opus Arte, a maker of DVDs. This year Opus Arte is planning to bring the ROH's opera and ballet performances to cinema screens across Europe (both pre-recorded and live) in partnership with Arts Alliance Media, a digital-technology company. These cinemacasts will be far cheaper than the Met's labour-intensive recordings, but their filming is far less elaborate and exciting, and the shows are rather like opera on television—albeit with a much bigger screen.

Sir Clive Gillinson, head of Carnegie Hall, New York's main concert hall, thinks cinemacasts are a brilliant tool to promote opera with all its theatricality, though he warns that it will soon be a very competitive market as a dozen or so of the leading opera houses are likely to be doing it. The big question now, he says, is how big is the market—and how much revenue is there in the long run?

Opera purists are not at all happy about Mr Gelb's foray into cinemas. They argue that opera was made to be seen live in opera houses and they worry that cinemacasts will hasten the demise of an ailing art form. The majority of opera houses across the world are under huge financial pressure, as governments are

increasingly unwilling to subsidise them.

Gérard Mortier, the head of the Opéra National de Paris, who spoke on filmed opera at the recent annual meeting of Opera America, a trade organisation, is the most vocal of the cinemacast opponents. He argues that his opera is reaching a far wider audience at much lower cost using good old television. The Met’s simulcasts did not work in French cities without an opera house, so they do not increase opera’s fan base. And young people shun cinemacasts because they are keen on live music, if they go to the opera at all. Next year Mr Mortier will take over as head of the New York City Opera, next door to the mighty Met. Expect a clash between the musical marketing wizard and the super-snob who likes to say that “art is anything but entertainment, and unrelated to box-office receipts.”

Business in France

Revolution, of sorts

Jul 3rd 2008 | PARIS
From The Economist print edition

Shareholder activism is taking off in France. But it has yet to achieve much

Illustration by David Simonds



WHEN Pardus Capital, an American activist fund, built a stake in Valeo, a French maker of car parts, its partners, Karim Samii and Behdad Alizadeh, frequently criticised the company's strategy. Local advisers told them to keep quiet. To get anywhere in France Inc, Pardus learnt, it needed to be polite.

Shareholder activism in France is on the rise. Several big firms, including Saint- Gobain, a building-materials firm, and Carrefour, a retailer, have recently accepted shareholders onto their boards. But even for the most well-mannered and long-established investment funds, trying to influence corporate strategy is proving controversial and difficult.

In French business circles *l'activisme* is almost a dirty word. Activists are seen as short-term asset-strippers trying to make a quick return. In the past a handful of wealthy individuals, such as Vincent Bolloré, a billionaire industrialist, mounted campaigns against companies. But the phenomenon of investment funds taking large stakes in big, well-known companies is a new one. Managers used to run things with no counterbalance, says Dominique Senequier, chief executive of AXA Private Equity, but now "it will become more and more usual for big shareholders to challenge the managers of companies which are underperforming."

Companies are not giving in easily, however. It took a prolonged war of words and a nasty public fight at the annual general meeting of Atos Origin, a computer-services firm, for Pardus Capital and a London-based hedge fund, Centaurus Capital, to win board seats at the end of May (Atos's chairman was also ousted). The funds argued that Atos Origin is too small to compete as a generalist, but too big to focus properly on a niche. Their eventual victory was hailed as the first for activist hedge funds in France.

But then a French private-equity firm, PAI Partners, suddenly appeared as Atos Origin's largest single shareholder two weeks ago, and said it backed the management's strategy. The hedge funds, however, are optimistic. "We know PAI well, we share the same DNA," says Bernard Oppetit, Centaurus Capital's chairman. "They are interested in maximising shareholder value, just like we are."

Mr Alizadeh at last won a single seat on Valeo's board in May, having asked for two. Now he has invited its other board members to dinner to discuss the firm, according to one of them (who does not plan to accept). Pardus may find it difficult to convince other board members of the need for change. Although Centaurus, which is run by former traders from BNP Paribas, the country's largest bank by assets, is reasonably well-regarded, Pardus, a foreign fund known for its abrasive style, is viewed with suspicion. But even though Pardus has just one seat, says a banker, people will pay more attention to Mr Alizadeh because of his firm's 19.7% stake.

Some investment firms reckon that in order to succeed as a shareholder activist in France, it is best to pretend not to be one at all. In the past few months Wendel, a listed, family-controlled investment firm at the heart of the French business establishment, has paid about €5.5 billion ($8.7 billion) for a 21% stake in Saint-Gobain, and this June it won three seats on its board. Wendel wants Saint-Gobain to cut costs and increase its presence in energy-saving products, but also says it supports the firm's strategy—a contradiction that may hamper its efforts to bring about change at the company, observers say.

Wendel's first foray into activism has gone badly. Despite the softly-softly approach, Saint-Gobain has

reacted defensively, and in May had to deny leaking information about Wendel to the French press. In June Wendel found itself under investigation by the French stockmarket regulator over the timing of its purchases of Saint-Gobain's shares. Worst of all, partly as a result of weak housing markets in several countries, Saint-Gobain's share price has plunged, so that Wendel's stake is now worth some €2.5 billion less than it paid—though the position is partially hedged, and the firm has no intention of selling in the near term.

Other activists have also been caught out by worsening economic conditions. Colony Capital, an American investment fund which specialises in property, and Bernard Arnault, chairman of LVMH, a French luxury goods firm, banded together last year to invest in Carrefour, the world's second-largest retailer. They now own a 10.7% stake. On June 26th the firm's shares fell by 9% when it cut its operating-profit target. The activists' main idea for Carrefour was to get the company to spin off part of its enormous property portfolio into a separate entity. But now that Carrefour's core business is under pressure, it may not be able to afford to lose the cushion of owning its own property and thus avoiding rent, says Philippe Suchet, an analyst at Exane BNP Paribas in Paris.

Colony has had greater success with Accor, a hotel group in which it holds a 17.5% stake jointly with Eurazeo, a private-equity fund. Accor has already sold a significant amount of hotel property.

Whatever the short-term headwinds for activism in France, its proponents are adamant that the phenomenon will only increase. “French business is open to outside investors and local activists alike, albeit grudgingly,” says Jean-Baptiste Toulouse, a managing director of Leonardo & Co., an investment bank. He points to comments from Claude Bébéar, honorary chairman of AXA, an insurer, and a leading figure in French business. In the midst of the fight over Atos Origin, he said that the hedge funds had a right to representation on the firm's board, given the size of their stake. Now that activists have successfully clawed their way onto boards, the next test will be whether they can make a real difference to the companies themselves.

Ambush marketing

Playing the game

Jul 3rd 2008
From The Economist print edition

Rival brands, as well as athletes, compete at sporting events

TAKING your hat off at the door may seem like a throwback to a more genteel age. But the practice lives on at modern sporting events. Dutch buyers of Heineken beer were given green hats to wear to the recent Euro 2008 football tournament. Anyone who tried to enter a stadium wearing one, however, as many fans did in 2004, was asked to remove it. The hats were an “ambush marketing” campaign, in which companies try to promote their brands at sporting events without paying sponsorship fees. Heineken’s rival, Carlsberg, was an official sponsor of Euro 2008, paying $21m for the privilege. A few TV close-ups of fans wearing Heineken hats would have cost very little by comparison. This was just one of 18 examples of ambush marketing at Euro 2008 identified by researchers at Coventry University Business School.

Ambush marketers have replaced hooligans as the villains of sporting events, because they undermine official sponsors, which are the main source of revenue in some sports. The stakes are highest at the Olympics. This year 12 firms, including Coca-Cola, Samsung and Visa, have paid a total of $866m to be official sponsors of the Beijing Olympics—and they want exclusivity.

The Chinese authorities have responded with their usual subtlety. Between July 11th and September 17th the Beijing Organising Committee for the Olympic games will take control of all prominent advertising sites in the Chinese capital, including those at train stations and airports, and their use will be limited to official sponsors only. (In 1996, when the Olympics were staged in Atlanta, the city was plastered with ads by Nike, which was not a sponsor.) Athletes will be banned from taking their own drinks into the Olympic Village to “protect sponsors’ rights”. And at each event if any spectators manage to get past the officials with unofficial food, drinks or clothing, broadcasters will be obliged to avoid showing them in close-up.

But preventing ambushes is difficult. Marketers tend to launch ambush campaigns only once an event has started, making pre-emptive strikes almost impossible. And policing the brand use of individual spectators at the stadium is tricky. Coca-Cola, which has sponsored every Olympiad since 1928, says sponsorship provides “a way to connect with people around the world at a very personal, emotional level”. But if that means depriving spectators of their half-finished Pepsi as they enter a stadium, the emotions may not be happy ones.

Overzealous enforcement can also result in bad press—as with the orange plastic *Lederhosen* given out by Bavaria, a Dutch brewery, to Dutch fans before a match at the 2006 football World Cup. Officials asked fans to remove the offending garments, to placate Budweiser, a rival beer brand that was the tournament’s official sponsor. Many fans ended up watching the match in their underwear, and the resulting fuss generated even more publicity for Bavaria.

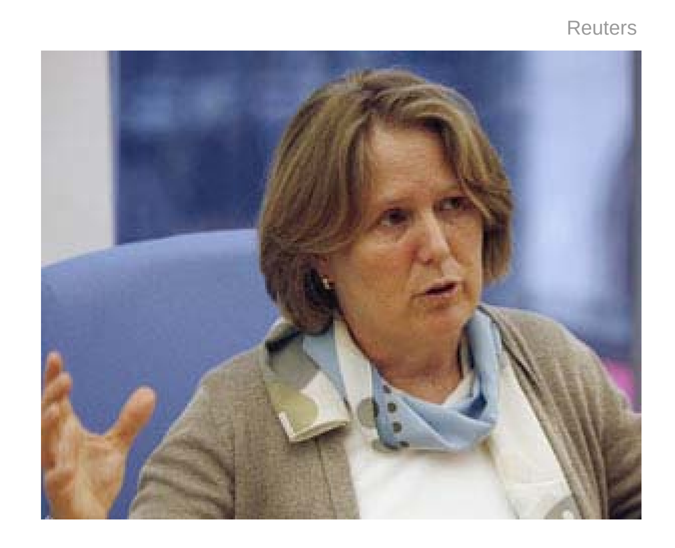
Face value

Virtual competition

Jul 3rd 2008
From The Economist print edition

Diane Greene of VMware favours co-operation over competition. Can she really keep Microsoft at bay?

Reuters



ALPHA male, flamboyant, brash, megalomaniacal. Profiles of leading high-tech bosses tend to be littered with these terms, signs of the traits that they seem to need to make it to the top of the computer industry and stay there. But none of them applies to Diane Greene, the chief executive of VMware. Her company, which sells software that makes data centres run more efficiently, has quietly become the world's fourth-most-valuable publicly traded software company, with a stockmarket value of nearly $20 billion. Its public listing last August was a bit like the heady dotcom days. Since then, the old guard has started ganging up on the newcomer, which boasts quarterly sales of nearly $440m and expects to grow by 50% this year. Microsoft, in particular, has vowed to take on VMware. On June 26th the software giant released its first competing product—predictably, as a free add-on to its flagship Windows operating system. How will Ms Greene play in the rough and tumble of the big league?

She has chosen an unusual route to the top of the software industry. After taking a degree in mechanical engineering, she wanted to work on oil rigs. But in the 1970s the offshore industry was still male-only territory. Even after a further degree in naval architecture she was allowed only to design huge oil platforms—not to visit them. At the time, however, things were getting exciting in a sport that occupied a lot of her spare hours: windsurfing. After organising several regattas, including the first world championship, and even winning some races, she moved to Hawaii in the early 1980s. "We had just discovered that you could make windsurfing boards out of fibreglass," she explains.

Feeling cut off from people and opportunities, Ms Greene returned to San Francisco's Bay Area to design commercial ships and windsurfing boards. Only then did she catch the computing bug, enrolling in 1986 at the University of California at Berkeley to study computer science. After a stint excavating a Spanish galleon and a few jobs at established technology firms, she ended up in the world of Silicon Valley start-ups. And in 1998 she helped her husband, Mendel Rosenblum, whom she had met at university, start VMware to commercialise the idea of "virtualisation". This divides a computer into several "virtual machines", allowing one computer to do the work of many separate ones, and thus helps companies make better use of their hardware.

To get an impression of Ms Greene's management style, you need only stroll through her company's new headquarters in the hills above Palo Alto. It goes without saying that the buildings are "green", with wooden benches in the corridors and photovoltaic panels on the roof. More important, the place is all about communication. Bridges connect the buildings, the cafeteria doubles as the central communications hub and every room has a glass wall. Ms Greene frequently grants interviews in a glass-walled meeting

room right next to the entrance—which she often nips out of to greet passers-by.

No wonder that the culture of VMware, which now employs over 6,000 people, is often described as open and collegiate. Where Ms Greene differs from the old school of high-tech bosses is how she sees the interplay between competition and co-operation. “I grew up playing Monopoly and Risk,” she says. “You have to collaborate to win these games—and compete when it is time to compete. But if you compete and break somebody’s trust you are going to lose the next time.” Maintaining trust means always being clear about what you are doing, she says, particularly since many of her firm’s partners are also rivals. What is more, Ms Greene argues, “With the internet, you can compete more effectively by being open.” When Microsoft tried to restrict how VMware’s customers could use its software with Windows, for instance, customers complained publicly and helped VMware prepare a white paper about Microsoft’s licensing practices that was posted online—after which the software giant relented.

Sadly, being open and playing nice has often been a recipe for losing against Microsoft. Even within VMware, some people observe that the co-operative approach often boils down to waffling. Others worry that VMware has not yet decided what game it is playing. Ms Greene’s plans for VMware do not sound terribly ambitious. In a nutshell, the company wants to turn virtual machines into “containers” for software and data. Firms can assign quality-of-service and security requirements to these software containers, and have them run wherever they want, be it on their premises or out in a computing “cloud”.

The opposite of Steve Jobs

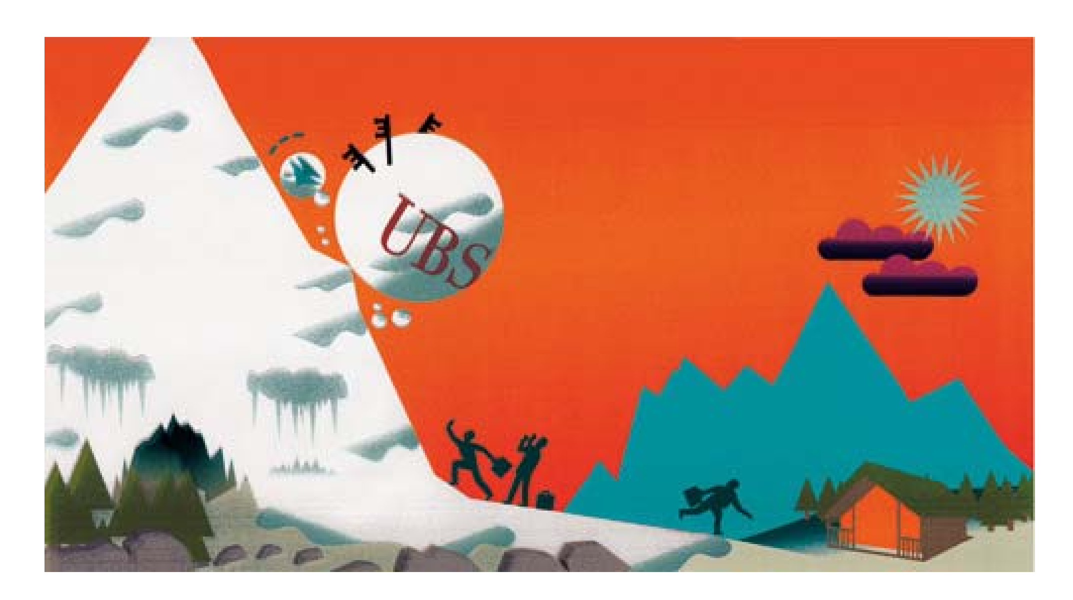
With her thinking on competition, however, Ms Greene may be onto something. To be sure, in the high-tech industry, competition and co-operation have always gone hand in hand. The phenomenon has come to be called “co-opetition”, but in the end, the competitive forces have always been stronger. However, as computing migrates into the cloud and becomes a service online, and as different pieces of software become ever more interconnected, then there is likely to be much more of a premium on co-operation. If computing used to be mainly about defending the citadel, it is now more about huddling with partners.

In which case, you would expect more high-tech companies to appoint leaders like Ms Greene. Indeed, that is one way of looking at the retirement of Bill Gates as Microsoft’s “chief software architect”, and his replacement by the more amenable Ray Ozzie. It is hard to imagine Mr Ozzie getting into public fights with Eric Schmidt, Google’s equally level-headed boss, the way Mr Gates did with Steve Jobs, Apple’s chief executive. Mr Jobs, by the way, will probably always remain something of an exception: his firm’s business today is still much more about control of the brand and the users’ experience than it is about co-operation. Interestingly, of all his colleagues in Silicon Valley, Mr Jobs is said to be particularly fond of Ms Greene. After all, opposites attract.

Swiss banks

Snowed under

Jul 3rd 2008
From The Economist print edition



Switzerland used to take pride in its big banks. Now it's not so sure

HAD Bradley Birkenfeld worked for a small Swiss bank, his tales of smuggling diamonds in a toothpaste tube—among other ways of helping American clients fool the taxman—would have merited only a line or two in the newspapers. But Mr Birkenfeld was employed until 2006 by UBS, Switzerland's biggest bank and the world's biggest wealth manager, looking after SFr2.8 trillion ($2.7 trillion). In his seven-page confession to a Florida court last month he claimed he was just a cog in a tax-evasion machine run by UBS. The world's press went to town.

For UBS the allegation—true or not—could not have come at a worse time. It is just one battle in the war to save its business model and perhaps its independence. Since April 1st, when it revealed that write-downs on its American mortgage-related assets had reached $38 billion, the bank has been fighting to sustain its share price and its credibility. This week the price dipped under SFr20, 70% below its peak in June 2007, as one leading shareholder dumped 2.3m shares.

There are rumours of more write-downs to come, thanks in part to UBS's exposure to threadbare monoline bond insurers. On July 1st UBS said it was getting rid of four members of its non-executive board, part of the old guard who saw the bank get into this mess. But they cannot be replaced until shareholders meet, on October 2nd. Change at UBS happens slowly: Marcel Ospel, the chairman who presided over its rise and fall, announced his resignation on April 1st and was replaced on April 23rd, but spent his last day at the bank only on June 30th.

Rumours abound that UBS, or parts of it, are for sale. On June 27th the bank felt obliged to deny rumours that it intends to sell PaineWebber, its American broker. Lazard, an investment bank, is advising it on a medium-term plan, which could involve a separation of investment banking and wealth management—a reversal of the "one bank" model propounded not only by UBS, but also by Credit Suisse, the other big Swiss bank.

In this model, investment-banking products are sold to wealth-management clients, and wealth-management products to investment-banking clients. This is fine in theory, but sceptics say the benefits do not justify the risks of running a high-octane investment bank. And these days, with greater demands for price transparency, there are fewer advantages to keeping the trades internal. "Investment banking and asset management might as well be separate," says a former UBS manager.

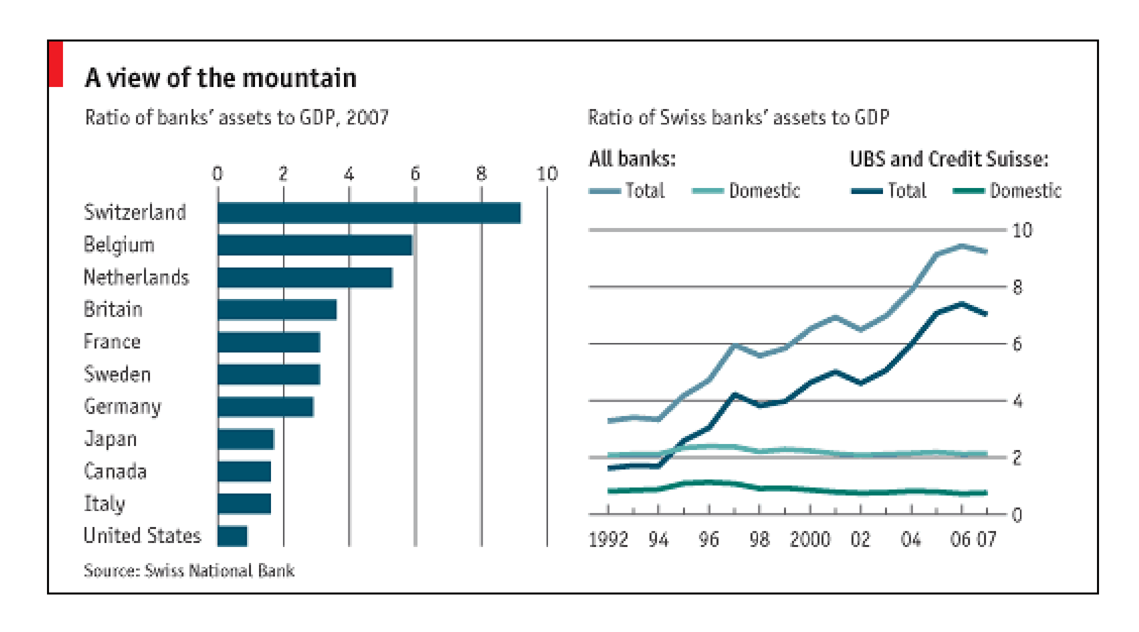
Much of these two banks' business, in trading and investment banking, is already conducted outside

Switzerland. Indeed, the Swiss Federal Banking Commission (EBK) has made no secret of the fact that it would be happy to see some of the high-risk investment banking go offshore, even if that means Switzerland loses rank as a global financial centre. If either UBS or Credit Suisse failed, the economy would be wrecked. To discourage any hope that the government would rescue either should it become insolvent, the Swiss deposit insurance scheme is capped at SFr4 billion per bank and covers only deposits held in Switzerland.

The EBK does not have the staff or skills to keep tabs on the big Swiss banks, although matters may improve with the creation of a new super-regulator next January, to be presided over by Eugen Haltiner, the EBK's chairman. It has generally relied on the maxim that Swiss banks should carry more capital than their foreign peers do, as a kind of insurance premium. But, like regulators elsewhere, it also put too much trust in the banks' own risk-based models. "The EBK has never said boo to the big banks," says a former UBS board member. It is hardly a good sign that Mr Haltiner worked at UBS until 2006 and used to report to someone now on its board.

However, the EBK's co-regulator, the Swiss National Bank (SNB), is now saying boo. It wants to strengthen risk-weighted capital measures that have been in operation, under the Basel 2 capital-adequacy rules, since the beginning of this year. It is also proposing a maximum "leverage ratio", a limit on the ratio of a bank's gross assets to its capital.

The suggestion is a slap in the face for both UBS and Credit Suisse. Their leverage ratios have grown dramatically in the past ten years. Philipp Hildebrand, vice-chairman of the SNB, points out that the two banks' combined assets amount to seven times Swiss GDP. In no other rich country do bank assets tower above the economy to such a degree (see chart).



Credit Suisse retorts that the leverage ratio is "outdated", because it ignores the risk-reducing effects of matching assets to appropriate liabilities. "We manage banks according to Basel 2, not Hildebrand 1," spat Tobias Guldimann, the bank's chief risk officer. A crude leverage ratio also makes no distinction between risky and stodgy assets—unlike Basel 2, which ties capital charges to the dangers of banks' positions. Measuring those risks is not easy, however. If risk models were perfect, there would be no need for a leverage ratio, "but they are not", says Mr Hildebrand. For what it is worth, Credit Suisse can claim that its models did slightly better than UBS's: so far it has sacrificed a mere SFr8.5 billion to the subprime crisis.

A maximum leverage ratio would certainly cramp the two big Swiss banks. Only Deutsche Bank, Germany's biggest, has a comparable capital-to-assets ratio. In America all regulated commercial banks already have to meet a leverage ratio, and will do so even when Basel 2 rules apply there from next January. Sheila Bair, chairman of the Federal Deposit Insurance Corporation, one of the many bodies that regulate American banks, insisted on it. Analysts at Keefe, Bruyette & Woods, an investment bank, say that UBS and Credit Suisse would have to shrink their assets by SFr500 billion and SFr300 billion respectively to meet American benchmarks.

Ideally, stricter rules on capital would be applied not in Switzerland alone but more generally, in order to prevent regulatory arbitrage. Basel 2 does allow national supervisors to add extra measures to improve a bank's risk management, but a harmonised approach is unlikely in the near term. For example, although American commercial banks are subject to a leverage ratio, American investment banks are not. And

differences in the accounting standards used in America and elsewhere lead to different leverage calculations.

If Switzerland did go it alone, the authorities would introduce the measure over the next few years rather than all at once, and exemptions would probably be made for mortgages and retail loans. And before getting to that stage the two big banks, especially UBS, first have to show that they have come through the crisis.

Thin end of the wedge

For Switzerland's smaller private banks the subprime difficulties experienced by UBS have so far been a boon: banks such as Julius Baer and Vontobel have seen money surge in over the past few months. But UBS's problems with the American authorities threaten Swiss banks as a whole.

America, the OECD and the European Union are always ready to attack the Swiss private banking model, with its notorious secrecy, as an unsporting competitor. Now UBS has given the American authorities an opportunity to demand details about banking clients. The Department of Justice (DoJ) and the Securities and Exchange Commission (SEC) are getting unprecedented co-operation from their Swiss counterparts, with the nice distinction that the Swiss will help in cases of tax fraud but not tax evasion. (Tax evasion is not a criminal offence in Switzerland.) Forgery of documents places the Birkenfeld file in the tray marked "fraud".

The DoJ is investigating whether UBS helped American clients avoid taxes. This week a judge ruled that the Internal Revenue Service (IRS) could require UBS to identify American taxpayers with accounts not declared to the taxman. The SEC is looking into a separate question: whether UBS's sale of American securities to American clients obliged it to register as a broker-dealer. Martin Liechti, a senior UBS banker, has been detained in Florida since April. Moreover, other UBS bankers from the Swiss-based unit which had been selling securities to American clients are no longer travelling to the United States. Other Swiss banks are also said to have stopped transatlantic trips.

At stake is UBS's status as a "qualified intermediary" (QI) under agreements, signed since 2001, between the IRS and foreign sellers of securities to American residents. At worst, UBS's QI status could be cancelled, making it virtually impossible for the bank to serve investors in America. UBS has said it is co-operating with these investigations.

Swiss officials were in Washington, DC, last month to assist the Americans. Avoiding confrontation is paramount, because American enforcers can exact punishment well beyond their own borders. Although the OECD has rather less clout than the United States, it does Switzerland little good to be on the organisation's list of places in which it believes too little is being done to combat "aggressive tax planning".

Germany also has Switzerland in its sights, in an investigation of data stolen from a Liechtenstein bank and bought by its secret service from the thief. Germany's offensive may be the more troubling: the Swiss have more to lose there, because America has proved a harder market for outsiders to crack. "[The German investigation] rocks the principle of client confidentiality to the core," says Sebastian Dovey of Scorpio Partnership, a consultancy.

Swiss bankers insist that they are fully compliant with international agreements and that banking secrecy is not absolute: they will breach it for cases of severe crime, such as money-laundering or financing terrorism. But they will not give out names and account data willy-nilly in response to "fishing expeditions", says Michel Dérobert, secretary-general of the Swiss Private Bankers Association. Swiss officials have been advising their American counterparts on how to extract information, given this constraint.

The big question is whether UBS can remain independent and intact. Banks that have slipped up have often become takeover targets. NatWest was devoured by Royal Bank of Scotland after making relatively minor errors in managing equity derivatives. The old Union Bank of Switzerland, after a similar gaffe, sought refuge with Swiss Bank Corporation, to form today's UBS. ABN AMRO, under attack by activists for its failure to provide shareholder value, was carved up by three predators.

UBS is in a worse state than any of those were: despite a world-beating wealth-management arm, its business model is dented and its board has not come up with a new strategy. Predators are rumoured to

be circling. What may save UBS is the generally sorry state of its industry: few would-be buyers have the ready cash for such a large deal. Hiving off divisions will also take time and money. UBS is more likely to soldier on alone, shrinking its business and licking its wounds. The newcomers on the board may help, of course, but they will not arrive until October. That seems a long way off.

Global markets

Bearish battalions

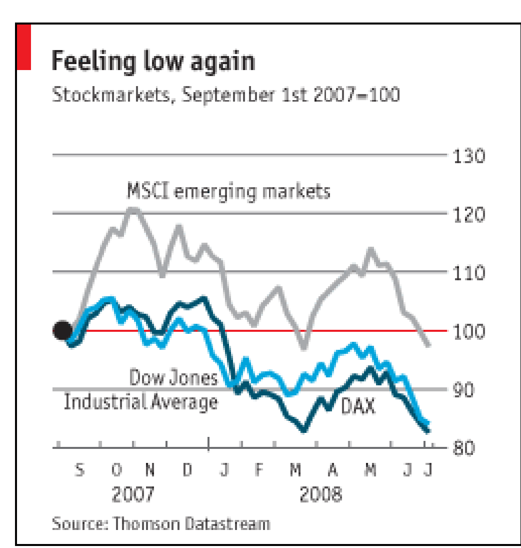
Jul 3rd 2008
From The Economist print edition

Illustration by Satoshi Kambayashi



Almost everything that could is going wrong for world stockmarkets

THEY rarely ring a bell at the bottom of bear markets. Investors who thought they had heard a tinkling sound when Bear Stearns, a failing American investment bank, was bundled into JPMorgan Chase in March have been disappointed. The Dow Jones Industrial Average is now weaker than it was in the spring (see chart).



The American stockmarket had its worst month since 2002 in June and is now down more than 20% from its peak, the definition of a bear market. It is not alone. According to Standard & Poor's, a rating agency, the value of global stockmarkets fell by $3 trillion during the month, thanks in particular to a 10% decline in emerging markets.

Share prices are suffering because of the outlook for four forces that impel stockmarkets: economic growth, profits growth, interest rates and inflation (see article). At the moment, the first two seem to be slowing while the last two are rising. That is the worst possible combination.

Soaring oil and food prices are stoking inflation. Oil closed at another peak of $144.14 a barrel on July 2nd, because of disappointing data on American crude reserves, and lingering fears that sabre-rattling between Israel and Iran might lead to conflict in the Persian Gulf. High commodity prices have also acted as a terms-of-trade shock for consuming countries—the things they buy from abroad cost more compared with the things they export. That has made them poorer.

The past six months could be seen as a dreary exercise in sharing out the pain. Will workers suffer by seeing their wages rise more slowly than inflation? Will companies have to compensate their workers by raising wages, sacrificing their profit margins? Will central banks treat high commodity prices as a blip, and leave real interest rates low, penalising savers? Or will they raise interest rates and risk pushing the economy into recession? None of these choices is palatable.

All this has been made worse by the credit crunch. True, the rescue of Bear Stearns seemed to avert the

implosion of the financial system. Credit spreads, which measure the excess interest rate paid by riskier borrowers, have fallen from their March peaks, although they have recently been rising again.

However, the crunch continues to chew its way through the system. Its effects can be seen in the sharp falls in mortgage approvals in both America and Britain. And it can also be seen in data produced by the Federal Reserve which show that loans made by banks (their assets, in the jargon) have fallen over the past three months.

This tightening in credit has taken so long to show up in the numbers because of the way that banks were operating before the summer of 2007. First, they had pushed much of their lending business off-balance-sheet, so that loans were bought by specialist entities like structured-investment vehicles (SIVs) and conduits. When the market for subprime loans collapsed, a lot of these loans came back on to the banks' balance-sheets. Second, banks had made back-up commitments to businesses to lend money if needed. With the collapse in other debt markets (such as asset-backed commercial paper), corporate borrowers cashed in those chips. Much as they would have wished otherwise, banks found their loan books expanding.

Now, chastened by the huge amounts of capital they have had to raise to strengthen their balance-sheets, banks are being more careful. According to Ian Harnett of Absolute Strategy Research, a consultancy, the availability of credit in Europe for both consumers and companies is now at its lowest level since 2003.

The problem for financial markets is that the virtuous circle which pushed asset prices higher in the middle of this decade may be turning vicious. Banks lend money against the collateral of assets, most notably in the form of housing. As house prices increase, the collateral rises in value and the banks are willing to lend more. That enables buyers to bid up prices even further.

But when banks stop lending, buyers are unable to purchase assets. Some investors are forced to sell to pay off loans. The value of collateral falls, making banks even more reluctant to lend. Markets freeze up, as neither buyers nor sellers have the confidence to do business.

As house prices fall in America, Britain, Ireland and Spain, the wealth effect kicks in. George Magnus, a strategist at UBS, cites the examples of Finland and Sweden in the early 1990s. As house prices fell, personal-savings rates jumped by 12-14 percentage points. A similar move in America or Britain would have a devastating effect on consumer demand, and thus on GDP growth over the next couple of years. As yet, there has been more of an effect on consumer sentiment than actual retail sales, although individual retailers (such as Britain's Marks & Spencer) are suffering.

As for companies, with consumers depressed and banks unwilling to lend, why should they invest? They may still see exports as a source of economic growth, but that works only for some firms in individual countries, not for those in the world as a whole.

So the market's sorrows have come in battalions, not single spies. Investors might have coped with the credit crunch if it were not for the high commodity prices, and vice versa. They do not know whether to fear inflation or recession more, but they know that both at once will be unpleasant.

It looks like a lengthy period of gloom is in store for the stockmarkets. Meanwhile, the best investors can do is hope, Micawber-like, that something will turn up. A collapse in oil prices would help.

Buttonwood

A gap in the hedge

Jul 3rd 2008
From The Economist print edition

Illustration by Satoshi Kambayashi



Owning shares is no shield against the scourge of inflation

IT IS easy to understand why bond markets are vulnerable to inflation, since the value of most bonds is fixed in nominal terms. But the remarkable thing about the inflation scare is that it has left them virtually unscathed.

The yield on America's ten-year Treasury bond finished June where it started in January, at around 4%. Perversely, bond markets have held up so well, it seems, because investors have perceived them as being low-risk. Instead, they have taken out their fears on the stockmarket.

At first blush, shares ought to be a good hedge against inflationary pressures. After all, inflation is a rise in the price of goods and services, and businesses make those goods and services. Their revenues should thus keep pace in real terms. In the jargon, equities are a real asset and bonds a nominal one.

But during the most recent period of high inflation, equities did not live up to their billing. Kevin Gardiner, a strategist at HSBC, says that real returns from American shares were just 0.1% a year from 1966-81; they fell a dismal 1.3% a year from 1973 to 1981.

Although that performance was much better than the painfully negative returns suffered by holders of government bonds, it was a long way short of the 6-7% returns that shares have historically achieved. Gold was a much better inflation hedge, earning an annual 10.9% in real terms between 1966 and 1981.

Why have shares been such a flimsy hedge? It was not that profits failed to keep pace with prices. According to Tim Bond, of Barclays Capital, business profits rose (marginally) in real terms during the 1970s in both America and Britain.

But simply keeping up with cantering inflation was not really good enough. As a share of GDP, American business profits fell from 12.2% in 1965 to 6.4% in 1982. They never touched that low again, rising fairly steadily to reach a temporary peak of 10.5% of GDP in 1997, before dropping sharply during the dotcom bust to 7.6% in 2001 and climbing smartly again to 11.8% in 2006.

Investors reacted to this long profits cycle by adjusting the stockmarket rating. In the 1970s shares were savagely downgraded, with price/earnings (p/e) ratios falling to single-digit levels. That explains the stockmarket's dismal performance.

In the long bull market from 1982 to 2000, stockmarket investors enjoyed the twin pleasures of soaring profits and expanding p/e multiples, which culminated in the dotcom bubble. But when the stockmarket rallied from 2003 to 2007, it was because of profits growth rather than a 1990s-style surge in multiples.

That could be a source of comfort. On the basis of trailing p/e ratios, shares look a lot more attractively valued than they did in 2000. (Much better to look at trailing, rather than prospective, earnings, because profit forecasts are still ludicrously high—investors are expecting a 20% rise in American earnings next year, according to Dresdner Kleinwort.)

But the problem is not the ratios; it is the earnings. If profits fall as a share of GDP all the way back to their 1982 low, or even to their 2001 nadir, share prices will suffer. Valuation measures that adjust for this, by using a ten-year average of profits, make shares look a lot less appealing.

The main question is why profits did so badly in the 1970s and whether those conditions are likely to repeat themselves. During those disorderly times, high inflation wrought enormous economic damage, making GDP growth, interest rates and company profits more volatile. (By contrast, the bull market of 1982-2000 coincided with the “great moderation” in economies.)

Figures from HSBC show that the “sweet spot” for the stockmarket is when inflation is between 2% and 4%. When inflation falls out of the bottom end of that range, the economy is normally flirting with recession and deflation. When inflation rises above 4%, and particularly when it reaches 6%, stockmarket valuations start to deteriorate sharply.

In the 1970s employers were unable to keep the lid on wage costs. That meant their margins took a double hit from rising raw materials and labour costs.

This time round, workers in the developed world seem to have less bargaining power. The risks of a 1970-style surge in inflation (and the accompanying slump in profits) are thus much lower.

But that may not be such a blessing for companies in the short term. For if workers see their real wages fall at the same time as the credit crunch is constraining their ability to borrow, consumer demand will suffer. Stockmarkets may well be retreating because, whichever way the inflation scare plays out, profits are sure to take a hit.

Regulating Wall Street

A window to a new world

Jul 3rd 2008 | NEW YORK
From The Economist print edition

The price of the Fed's lifeline is yet to be determined

FOR an industry that has seen many a defenestration over the past year, you might expect America's investment banks to be wary of open windows. But the move in March to allow primary dealers as well as commercial banks to borrow overnight from the Federal Reserve's discount window has calmed fears of further Bear Stearns-like death spirals. Lehman Brothers, the weakest of the remaining big investment banks, may have seen its share price pummelled as questions swirl over its business model. But no one thinks it is about to run out of cash.

What will this lifeline cost in terms of regulation? That may be clearer after Congress holds hearings on the issue, scheduled to begin on July 10th. Wall Street executives are not optimistic. "The favourite game on Capitol Hill these days is Hunt the Investment Banker," sighs one.

Initially opened for six months, the window will almost certainly be kept ajar when that period ends in mid-September, given the continued market instability. Lehman is not alone in being glad of the protection. Merrill Lynch faces further write-downs and may report another quarterly loss in mid-July. Even Goldman Sachs, Wall Street's sole surviving muscleman, sees the loan facility as systemically crucial. Though the amount borrowed has fallen to a daily average of $6 billion, closing it would cause "mayhem" by inviting speculative attacks, particularly against Lehman, reckons another banker.

The first piece of the *quid pro quo* is already in place. By sending teams of officials into the investment banks, the Fed has in effect usurped the Securities and Exchange Commission (SEC) as their main regulator. The two are working on a formal agreement that will clarify how they share information, and give the Fed greater access to the banks' trading positions. The future division of responsibility remains unclear, however. The likeliest outcome is a double-headed regime, with the Fed as a stability regulator for large financial institutions of all types, and the SEC policing investor protection. But Christopher Cox, the SEC's chairman, is under pressure—both internally and from several predecessors—not to cede ground.

This looks like just the beginning of the shake-up. "We lack appropriate constraints on risk-taking at investment banks," says Barney Frank, the head of the House financial-services committee. Mr Frank wants Wall Street to be subjected to capital requirements similar to those for stodgier commercial banks (which are lobbying vociferously for the gap to be closed). But investment bankers argue that this would put them at an unfair disadvantage, since they have to mark their assets to market, whereas commercial banks can hold large chunks at historic cost.

As well as being coaxed into reducing leverage, the banks may face pressure to ditch some of their illiquid assets, such as mortgage-linked securities and private-equity stakes. Regulators are said to be mulling an "aged inventory capital charge", which would penalise banks that held paper for longer than, say, one month. Another proposal is to limit their venture-capital and hedge-fund holdings. Yet another would raise the capital charge on loan commitments.

Funding is under the spotlight, too. Investment banks have already rushed to reduce their reliance on overnight funding in repo markets, after lenders lost faith in the securities used as collateral. Regulators want to encourage more long-term funding and deposit-taking. Though stable, however, deposits are a more expensive form of finance than repo markets for banks that lack branch networks.

The banks' balance-sheets are not the only cause for concern. There is also no clear mechanism for winding down a failing investment bank. Sheila Bair, head of the Federal Deposit Insurance Corporation, has suggested extending the "bridge bank" model already in place for commercial lenders—which maintains key businesses while selling off assets. In a speech this week, Hank Paulson, America's treasury secretary, placed this issue at the top of his agenda.

None of this will be good for Wall Street's profitability. Analysts expect the industry's return on equity to fall by a third or more over the cycle. Bob Gach, head of the capital-markets practice at Accenture, a management-consulting firm, thinks the new shackles will hasten the demise of the stand-alone investment bank—though Goldman and, to a lesser extent, Morgan Stanley may remain as exceptions. In a recent op-ed article, Mr Cox looked forward to a "brave new world" of financial regulation. For Wall Street's erstwhile high-fliers, it will be an unsettling one.

The Bank for International Settlements

Settling scores

Jul 3rd 2008
From The Economist print edition

If the BIS is right, inflation is a more immediate threat than deflation

IT IS always satisfying to be proved right, even when your prediction was that things would go horribly wrong. For years the Bank for International Settlements (BIS), the Basel-based bank for central banks, warned policymakers that they were not paying enough heed to the rapid growth in borrowing. The bursting of credit and house-price bubbles in America bears out the analysis of William White, the BIS's sadly retiring chief economist, who has long argued that interest rates were being held too low. In its annual report, published on June 30th, the BIS leaves readers pondering what the penalty for lax policy will be: inflation or deflation.

Credit busts often beget recessions. During the last big recession in the rich world, in the early 1990s, the economies that fell hardest were those whose household debt had risen most. The BIS reckons debt burdens and falling home values will again combine to push down GDP growth. As consumers cut back on spending to pay off their debts, there could even be deflation. But, as its report notes, the long period of low global interest rates that lifted house prices and borrowing has also fuelled inflation. Central banks that rely on the credit crunch to tame rising prices may regret it.

Because inflation is the immediate threat, says the BIS, there should be a bias towards tighter global monetary policy. But there is no universal prescription: each central bank must weigh the local risks that inflation will persist against the threat of deflation from overhanging debt and fragile banks.

The acute dilemmas facing policymakers make the BIS's call for a new policy framework to prevent future bubbles all the more relevant. Reforms will be less useful if they focus on the triggers of the crisis—the packaging of unsound mortgages into exotic securities sold as safe investments—rather than its underlying causes.

Like previous blowups, the credit crunch has its roots in short-sighted monetary policy and in the tendency for bank lending, rising asset prices and strong GDP growth to reinforce each other. So central banks and bank regulators need to act in concert to temper the credit cycle. That may ultimately mean raising interest rates, even when the immediate outlook is for low inflation. But that is a long way off yet.

Debt relief

Waiving, not drowning

Jul 3rd 2008 | SIKANDRABAD
From The Economist print edition

India writes off farm loans. Has it also written off the rural credit culture?

A KNOT of farmers points in anticipation and dread at the spreadsheets posted on the walls of a bank in Sikandrabad, a small town in Uttar Pradesh, India's most populous state. The suspense is heightened for those who never learnt to read their own names, at least not in the Roman alphabet. The print-outs list 419 farmers, out of about 43m nationwide, whose debts were excused or discounted on June 30th, in the biggest write-off in India's history.

The loan waiver, which will cost 1.6% of GDP, was unveiled by the finance minister, Palaniappan Chidambaram, in his budget in February. Back then, when oil prices were a mere $100 a barrel, he calculated he could spare $17 billion or so to ease the distress of India's small farmers and shorten his government's odds of winning the next election, due by May 2009. A few months earlier, an expert group on rural indebtedness had provided a long list of worthy proposals, such as organising farmers into self-help groups, and employing satellites to forewarn farmers of unkind weather.

But the government decided that a far quicker and easier way to help them was to let them off their debts. After all, their names and liabilities were already on bank ledgers. So it ordered many banks and credit co-operatives to forgive farm loans by June 30th, and promised to compensate them in instalments over four years. Shares in the State Bank of India, 60% of which are owned by the government, have lost half their value since the waiver was announced.

In Sikandrabad one farmer could not quite believe that the pink slip he had been given released him from 25,000 rupees of debt. But others did not get the result they were hoping for. The scheme distinguishes between "small" farmers with less than five acres, and "other" farmers with bigger landholdings. Small farmers will have their debts forgiven; others will have them cut by 25%. Spare a thought then for the local farmer with 5.12 acres and a debt of 8,368 rupees to his name.

Harlal Singh could not find his name on the wall—and not because he could not read. On the contrary, he has written plaintively to the finance minister and to Rahul Gandhi, son of the Congress party's leader. Mr Singh's mistake was to take a loan in June 2007, when the waiver applies only to loans made by March 31st of that year.

The branch manager has heard other grievances, especially from those who repaid their loan too soon. "Those people are angry," he admits. "They say: 'We were honest and got nothing; those who were dishonest got their loan waived.'"

Some fear the government's largesse will do lasting damage to a culture of prudent borrowing, productive investment and prompt repayment. The last time India tried a nationwide write-off in 1989-90, it had the perverse effect of making banks reluctant to lend to the poor, argues Vijay Mahajan, chairman of BASIX, a microlender, in an interview with a newsletter of the Centre for Micro Finance in Chennai.

He argues that villagers have learnt to distinguish between soft government credit, which is haphazardly administered, heavily subsidised and often forgiven, and private loans, which are offered, monitored and collected with greater diligence. In fact, he says, they often use different words for the two kinds of "loan". The English word is used for soft loans from the government; local words are used for loans they should take more seriously. By stepping in to waive loans made even by commercial banks, the government may have blurred the distinction.

Right now, a precarious government is more concerned about getting due credit at the ballot box. It hopes its $17 billion eraser will result in millions of votes. But if his letters go unanswered, Mr Singh for one is going to vote for the other guy.

Leveraged buy-outs

Private investigations

Jul 3rd 2008
From The Economist print edition

Our calculations suggest buy-out firms may come to rue some of the “mega-deals” they did when pumped up with self-belief

IN FINANCE, as in Greek tragedy, one of the commonest pairings is between hubris and sheer, toe-curling folly. In the boom years of 2006-07 nothing, it seemed, could constrain the leveraged buy-out (LBO) industry. In 24 months it pulled off deals with an enterprise value of $1.4 trillion, the equivalent, after adjusting for inflation, of about a third of all the buy-outs ever done. Thanks to the credit crunch, buy-outs have since become scarce: so far this year only $131 billion of deals have been announced, according to Dealogic. Yet those expecting private-equity executives to be cowering in fear of retribution will be disappointed. The mood remains one of almost hypnotic confidence.

Is this justified? On June 26th Chrysler, an American carmaker bought by Cerberus, a private-equity firm, in one of the highest profile deals of last year, felt obliged to deny it had filed for bankruptcy. Banks are selling loans made to LBOs at big discounts, reflecting wider fears of default. Other “mega-deals” that had not quite closed before credit markets froze last summer are suffering from a collective loss of nerve. Shareholders of Clear Channel Communications, an American media firm, will on July 24th vote on a revised offer with a lower price and debt level. The bidders for BCE, a Canadian telecoms operator, are still haggling over terms with their reluctant banks.

The Economist has examined ten of the biggest completed LBOs that were announced in 2006-07, accounting for a fifth of the total by value. Two are already home and dry. Blackstone, a private-equity firm, profitably sold on most of the property assets of Equity Office Properties within months of buying it. On June 5th buy-out funds run by TPG and Goldman Sachs sold Alltel, an American cellular operator to Verizon Wireless at a slight premium. But the condition of the eight others is less reassuring. In the latest quarter three of them suffered year-on-year declines in sales or underlying operating profits or both, mirroring the broader pressures on company profits. Under such conditions, the ability to make money for investors is one question; whether the biggest deals can survive with such huge debts is another.

Bankruptcy has been a feature of previous buy-out binges. Steven Kaplan, of the University of Chicago, reckons that about a quarter of the large deals struck between 1985-89 eventually defaulted. Today the eight mega-deals that are still in the hands of their original acquirers have balance-sheets that by any reasonable standard leave no margin for error. On a weighted-average basis, after allowing for capital expenditure, cashflow only just covers interest payments (see table). Listed companies, even after excluding those in the booming energy and mining industries, have interest cover nearer to ten times, according to UBS’s World Inc database. If public firms are equipped to withstand a storm, LBO balance-sheets, it would seem, could barely cope with a summer shower.

Je ne regrette rien

Top-ten completed buy-outs announced in 2006-07

Target	Bidder/s	Deal enterprise value (EV), $bn	2007 Pro-forma net debt, as a % of EV	2007 Interest cover*
TXU	KKR, TPG, Goldman Sachs	43.8	89.5	0.5
Equity Office Properties	Blackstone	38.9	largely sold	largely sold
HCA	Bain, KKR, Merrill Lynch	32.7	82.4	1.6
Alltel	TPG, Goldman Sachs	27.9	sold	sold
First Data	KKR	27.7	79.2	1.0
Harrah's Entertainment	TPG, Apollo	27.4	83.7	0.8
Hilton Hotels	Blackstone	25.8	75.9	1.1
Alliance Boots†	KKR	20.6	83.5	1.1
Freescale Semiconductor	Blackstone, Permira, Carlyle, TPG	17.6	49.6	1.6
Intelsat	BC Partners	16.4	88.9	1.0
Weighted average	–	–	81.0	1.0

Sources: Company reports; Dealogic; *The Economist* estimates

*2007 EBITDA minus capital expenditure, divided by estimated pro-forma interest †Year ending March 2008

Nonsense, say private-equity executives, who believe that they still have plenty of room for manoeuvre. Firstly, some of those firms bought in the big transactions have rapidly rising profits, allowing them to rebuild their interest-cover ratios. Hilton Hotels, for example, is performing ahead of its targets, buoyed by its exposure to growing markets outside America. Sales at Intelsat, a satellite operator, are rising at a double-digit pace. Alliance Boots, a European drugs retailer, confounded its critics by announcing a healthy rise in operating profits in June. Secondly, even those firms facing tougher trading conditions have flexibility, because they can cut capital expenditure. Were Harrah's Entertainment, a casino operator, to cut capital spending to "maintenance" levels sufficient just to keep the business running, its interest coverage would rise from an estimated 0.8 times to a less sweaty-palmed 1.3 times. Freescale Semiconductor, an American firm, has already cut back investment.

Even more comforting, say private-equity executives, is the legacy of the extraordinarily generous credit terms they won before the credit crunch struck. Most of the eight remaining mega-deals have weak covenants and "payment-in-kind" arrangements that allow them to defer cash interest payments, in one case for up to one-fifth of the total. Some also have plenty of liquidity: Harrah's has cash and unused bank facilities equivalent to two years of interest payments. If push comes to shove, buy-out funds could inject some of their "dry powder" (money raised but not yet spent) to pay down debt—providing the conflicts of interest between new and old investors could be managed. What is more, there is plenty of time before principal payments kick in: typically, five years or more. Stephen Schwarzman, chairman of Blackstone, argues that his firm's acquisitions have "bomb proof" capital structures. By quoted company standards, that is an exaggeration. But at least the mega-deals do not look as if they are in imminent danger of going bust.

Survive but not prosper

If that is some comfort for their lenders, there is far less reassurance for investors in private-equity funds. Again, history is one reason for pessimism. Data from Cambridge Associates show that American private-equity funds raised during the previous boom years of 1987-88 and 1997-99 typically generated a median internal rate of return (IRR) of about 11%. That is poor given the high leverage that buy-out firms took on and well below the 20%-plus median returns for funds active in the dark days after the 2000 stockmarket crash.

Staggering under too much debt is bad for companies' performance: capital-expenditure cuts can damage future growth and competitors may react by starting price wars (as Philip Morris, a rival tobacco company, did following the RJR Nabisco deal). And one of the tricks used to enhance IRRs in recent years, paying special dividends funded from even more borrowing, is no longer an option given credit-market conditions. Nor are valuations encouraging. The eight outstanding mega-deals were bought on a weighted-average price/earnings ratio of 24 times, well above where stockmarkets trade now. In some cases the share prices of quoted peers have tumbled as the outlook for profits has darkened.

Irrelevant, say some industry supporters. After all, investors in private-equity funds are typically locked in for at least five years and no one plans to sell now. Most of the mega-deals involved companies with high market shares and good brands: exactly the sort of businesses that can prosper in a downturn. What is

more, it is argued, if mark-to-market losses do exist, they may not have to be recognised. Indeed, although notionally subject to accounting rules that require investments to be carried at fair value, private-equity firms seem to enjoy a degree of latitude that most bank executives would kill for. The disclosure remains hazy, but it appears that Freescale is the only one of the top-ten deals in which the carrying value has been written down much below cost.

Yet having a long time horizon does not make the present of negligible importance. Based on today’s outlook, just how bad might LBO losses be? One clue comes from two Dutch-listed entities, run by Apollo and KKR, that have invested part of their capital in their sponsors’ buy-outs. Their shares now trade at discounts of over 45% to the net asset values booked in the first quarter, suggesting deep scepticism that these investments are still worth what was paid for them.

That is not to say some private-equity firms will not have the last laugh. Historically the best time to invest in LBOs has been after what Mr Schwarzman calls “meltdown years”. Despite tricky markets private-equity firms have closed huge new funds in recent months. Investors must be hoping their cash is spent more wisely than in the recent past.

Economics focus

The domino effect

Jul 3rd 2008
From The Economist print edition

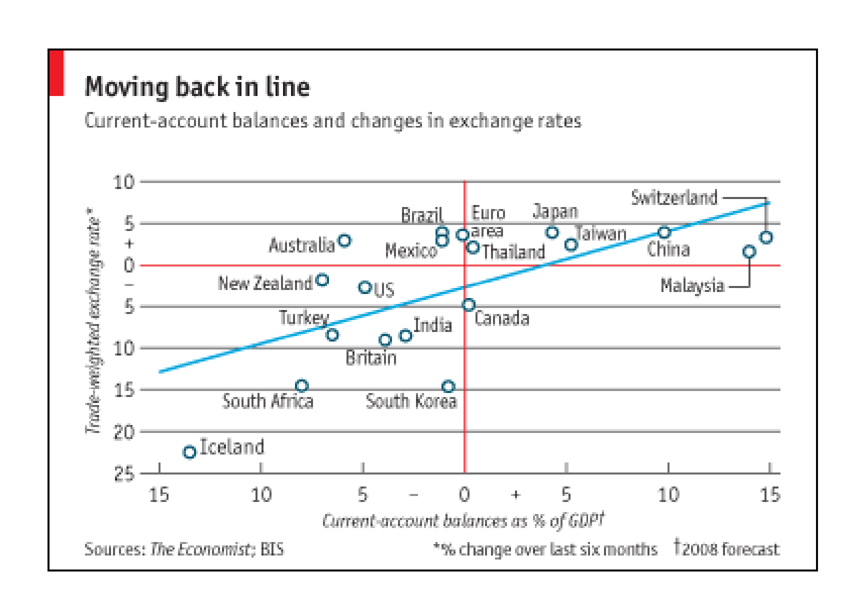
Many currencies that are backed by a current-account deficit are now falling just as the dollar has

ACCORDING to economic textbooks, the currencies of economies with large current-account deficits should depreciate relative to those of countries with surpluses. This will stimulate their exports and curb imports, thereby helping to slim the trade gaps. America has the world's biggest current-account deficit and the dollar has dutifully been falling since 2002. Oddly, however, the currencies of many other countries with large deficits had enjoyed big gains until recently. Now, at last, currency markets have started to see sense.

Britain, Australia, New Zealand and Iceland all have large current-account deficits (along with many other American-style excesses, such as housing and credit booms). Yet over several years until mid-2007, their currencies perversely rose relative to those of economies, such as Japan and Switzerland, with big surpluses. For example, despite a current-account surplus of 4.9% of GDP last year, one of the biggest of any developed economy, Japan's trade-weighted exchange rate sank by 13% from the end of 2002 to mid-2007. New Zealand, where the deficit reached 8% of GDP (bigger than America's deficit of 6% of GDP at its peak), saw its currency gain 28% over the same period.

This paradox is the result of the "carry trade", a popular currency strategy that partly explains why trade flows are now dwarfed by cross-border capital flows. In a world of low interest rates, international investors were hungry for yield, and so piled into currencies that offered higher interest rates, namely those of Britain, Australia, New Zealand and Iceland, as well as many emerging markets. Those higher interest rates paid by countries with large external deficits were supposed to compensate investors for the risk of currency depreciation. But as investors borrowed in low-interest currencies, such as the yen, to invest in high-yielding ones, this made the latter currencies stronger. That, in turn, prolonged global imbalances by making it easier for profligate countries to finance their current-account deficits.

But since the eruption of global financial turmoil last year and the dwindling appetite for risk, carry trades have started to unwind and it has become harder to finance deficits. As a result, current-account imbalances are once again exerting a powerful influence over currencies. The chart shows that the weakest currencies this year have been in countries with deficits, from Britain to South Africa. In contrast, the yen and the Swiss franc have perked up. The same chart a year or so ago would have shown virtually the opposite relationship.



Increased concern about current-account deficits is also causing investors to discriminate much more

between emerging markets. A popular argument in recent years has been that developing economies are less risky because, unlike a decade ago, they are no longer dependent on foreign capital. It is true that emerging economies are forecast to have a combined current-account surplus of more than $800 billion this year, but this is more than accounted for by China, Russia and the Gulf oil exporters. In fact over half of the 25 biggest emerging economies now have deficits. South Korea is running a deficit after a decade of surpluses. Brazil has also moved back into the red, despite record high prices for its commodity exports. Others such as India, South Africa and Turkey have had external deficits for many years.

Sticking to our “mercantilist” guns

In an article last November, *The Economist* ranked 15 of the biggest emerging economies according to their economic riskiness. Based on the size of external and budget deficits, inflation rates and the pace of growth in bank lending, India, Turkey and Hungary were deemed to be most vulnerable. The ranking attracted a lot of flak in India. An article in the *Times of India* accused *The Economist* of “mercantilist thinking at its worst” by treating a current-account surplus as good, a deficit bad. Agreed, a current-account deficit is not necessarily bad: an economy may be borrowing from abroad to finance investment that will lift future growth. Nevertheless, a large deficit does mean that an economy and its currency may struggle if foreign-capital inflows suddenly dry up.

And this is what has happened. This year foreign capital has gone into reverse at the same time as India’s current-account deficit has widened sharply. Sharmila Whelan, an economist at CLSA, a brokerage firm, forecasts that India’s current-account deficit will rise to almost 4% of GDP in the current fiscal year, and to 5.5% next year. Not only is the trade deficit soaring, largely as a result of higher oil prices; the overseas earnings of Indian IT services companies (two-fifths of which come from the financial sector) are likely to shrink this year.

The nature of the capital inflows financing a deficit also matters. Foreign direct investment (FDI) is less volatile than speculative capital inflows. If we assume that net FDI continues at last year’s pace, then it would more than finance the expected current-account deficits in Brazil and Mexico this year. In contrast, net FDI might finance less than one-third of India’s deficit and only one-sixth of South Africa’s, implying that their currencies are more at risk. The rupee has fallen by almost 10% against the dollar since late last year. Ms Whelan forecasts that it will drop by another 9% by March 2009.

Central banks in the developing world are now worried that falling currencies will exacerbate inflationary pressures. A year ago most emerging economies were intervening heavily to hold their currencies down; now many in Asia, including India, South Korea, Vietnam and Thailand, are having to sell dollars to prop their exchange rates up. The prime exception is China, where hot money continues to pour in and where the current account has a massive surplus.

The longer that international investors remain risk-averse, the more attention they are likely to pay to current-account imbalances. A few currencies seem to have been overlooked: those of Australia, Poland and Hungary have so far held up surprisingly well, despite their gaping external deficits. All three now look overvalued. They could be the next dominoes to fall.

Regulating pesticides

A balance of risk

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From The Economist print edition

Getty Images



Pesticides keep food edible and cheap. On the other hand they are, by definition, poisonous. Europe's legislators thus face a dilemma

WHAT is the difference between risk and hazard? Quite a lot, it seems, if you make or use pesticides. Everybody hates them (dangerous, unnatural things). But everybody likes their benefits (cheap and unblemished food). Sensibly regulating their manufacture and use is thus a minefield—but one that Europe's politicians and bureaucrats are now attempting to cross without getting blown up.

The difference between hazard and risk, in this context, is that hazard is something you measure in a laboratory by finding out how much of a substance you need to kill or injure an experimental animal. Risk is something you measure in the real world. Risk depends not just on how toxic a chemical is, but on how it is actually used, how much of it is used and how often it is used. At the moment, Europe's rules on pesticides are based on risk. However, a piece of legislation regulating plant-protection products, which is awaiting its final reading in the European Parliament later this year, will shift the basis of the law towards an assessment of hazard.

The legislation's supporters claim it will lead to some of Europe's most hazardous chemicals being withdrawn from the market. Wolfgang Reinert, an official at the European Commission's directorate on Health and Consumers, says the new rules embrace the philosophy that something should be for sale only after the producer has proved it can be used safely.

Many agricultural scientists, however, argue that the change will have widespread, alarming consequences for farming, and will lead to further increases in food prices at a time when they are already uncomfortably high. ADAS, a British environmental and rural consultancy, has produced a report which says even the lowest-impact proposals would reduce food production by a quarter. In January an Italian report came up with a similar figure.

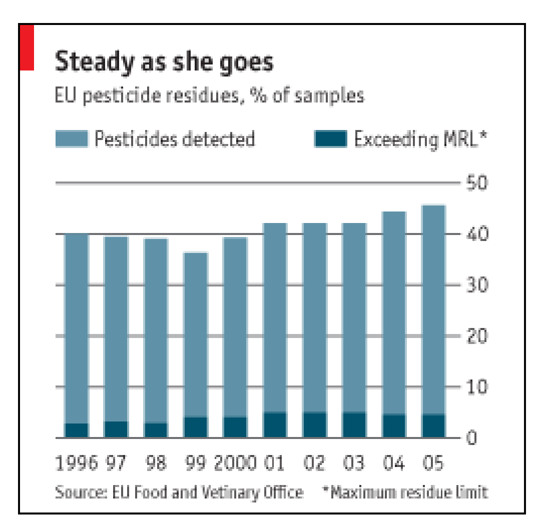
Taking-cides

The threat to the use of pesticides is certainly serious. Depending on exactly how it is enacted, the legislation could outlaw all but one of the pyrethroids, a widely used class of insecticides; triazole, a fungicide used to protect cereal crops; and dithiocarbamate, a herbicide that controls a cereal-strangling weed called black grass. Yet all of these hazardous substances pose little risk if used properly.

Not surprisingly John Atkin, the head of the crop-protection part of Syngenta, a Swiss agrichemical and seed company, believes the changes are wrong. As he puts it, “current regulations are tough and we have already reached a point where some useful compounds, particularly for minor crops, have been lost, to the detriment of agricultural productivity.” (The minor crops in question include leeks, green beans and flower bulbs.) He adds that even under the existing rules some 700 substances have disappeared from the market, out of an original total of around 1,150.

Others without a commercial axe to grind agree with him. Ian Dewhurst, the principal toxicologist at the British government’s Pesticide Safety Directorate, points out that by failing to think about real-world risks, the European Union may end up acting against the wrong pesticides. It is not merely that the EU will probably ban what is, in practice, safe, but also that it might let through what is causing the most harm. Ian Denholm, head of plant and invertebrate ecology at Rothamsted Research, an agricultural institute in Britain, agrees, and judges that the present system, founded on science-based risk-assessment, is a “rigorous gold standard”.

The counter-argument is that, gold standard or not, the existing legislation (which was drafted in the late 1980s) is not working. As the chart shows, the share of food samples that exceed the maximum residue limits (MRLs) in Europe has remained constant for many years. Elliott Cannell, a spokesman for the Pesticide Action Network, an environmental group based in London, reckons the average European probably eats food contaminated with pesticides at least once a fortnight. The virtue of a risk assessment is that it captures what happens in the real world. If it fails to capture the actual threats to health, as these results suggest is happening, then it is failing to do its job.



Vyvyan Howard, a toxicologist and pathologist at the University of Ulster, and a supporter of the reform, also reckons that the existing system is not as good as it claims to be. He says it assesses exposure on a complex model of the world that is not always correct. “We know,” he says, “we get pesticides turning up where we don’t expect them.” He points to the example last month of gardeners in Britain being warned not to eat home-grown vegetables after manure they might have used became contaminated with a herbicide called aminopyralid.

The new system, according to Dr Howard, is based on science, but with pragmatism. The idea is to reduce the overall toxicity of the entire armory of pesticides. The new criteria would remove the most hazardous products from the food chain altogether. He believes this is particularly important for protecting fetuses, whose development is especially susceptible to disruption by outside chemical signals.

Just dilute before use

Science, however, is one thing. Politics is another. In response to the sceptics’ concerns, Europe’s agriculture ministers met on June 23rd to hammer out a compromise that will allow any country that feels it cannot replace a particular pesticide to ask permission to continue to use it. This has angered green groups and it has pleased neither agricultural scientists nor the British government. The exemption, Dr Denholm reckons, is “totally worthless”. The job of obtaining an exemption, he says, is too bureaucratic and could involve as much as two years of consultation.

One lesson from all this is that you cannot please all of the people all of the time. Cheap, pesticide-free food is probably an unachievable objective. The other lesson, however, is that science—so often seen as a way of arriving at clear-cut answers—is itself a process of muddling through to the truth. Hazard assessment has a certain purity, but that purity is often irrelevant to real risk. On the other hand, a true risk assessment is impossible, since not all of the variables can be identified, let alone measured and modelled.

But perhaps there is one lesson that science still can offer the politicians. It is this: by all means do the experiment and find out. But, if the experiment fails, have the guts to admit you were wrong and try something else. Politics being what it is, the new legislation is certain to be introduced. If it turns out to be a costly mistake, it should not be allowed to last.

Wine and health

Of sommeliers and stomachs

Jul 3rd 2008
From The Economist print edition

Red wine exercises its benefits before it enters the bloodstream

FINE food sings on the palate, but pairing it with the right wine creates a chorus. Among those in the know, the plum, chocolate and spice flavours of Cabernet Sauvignons, Merlots, Pinot Noirs and Sangioveses best accentuate the rich flavours of red meats. Now, however, a group of researchers led by Joseph Kanner of the Hebrew University of Jerusalem has discovered that pairing red wines like these with red meat appears to be more than just a matter of taste. If the two mix in the stomach, compounds in the wine thwart the formation of harmful chemicals that are released when meat is digested.

The idea that red wine is actually good for your health is irresistible to the average tippler. But it appears to be true. In particular, red wines are rich in polyphenols, a group of powerful antioxidants that are thought to protect against cancer and heart disease by destroying molecules that would otherwise damage cells. How the polyphenols in wine exercise their beneficial effects, though, has been mysterious. That is because they do not seem to travel in any quantity from the stomach into the bloodstream.

The answer, Dr Kanner has found, lies in the stomach itself. The digestion of high-fat foods such as red meat releases oxidising toxins. One in particular, called malondialdehyde, is implicated in arteriosclerosis, cancer, diabetes and a host of other serious diseases. Dr Kanner suspected that the key to wine's protective effect is when, precisely, it is consumed. He hypothesised that if the polyphenols arrive in the stomach at the moment when the fats are releasing malondialdehyde and its kin, then this might stop these toxic materials from getting any farther into the body.

To test this idea, he and his colleagues fed a group of rats one of two meals—either red meat from a turkey (a foodstuff shown by previous research to raise malondialdehyde levels in humans) or such meat mixed with red-wine concentrate. An hour and a half after the rats had eaten, they were killed. Dr Kanner then removed their stomachs and analysed the contents. As he reports in the *Journal of Agricultural and Food Chemistry*, the wine concentrate did indeed reduce the formation of malondialdehyde. It also cut the level of hydroperoxides, another group of oxidising agents that cause cell damage.

Based on these results, Dr Kanner and his colleagues argue that looking for antioxidants from wine in the bloodstream was a mistake; they do not need to be there to be useful. Their research also suggests that the habit of eating fruit at the end of a meal is a healthy one. Many fruits, too, are rich in polyphenols (wine is, after all, just fermented fruit juice). By treating them as dessert, these fruits arrive in the stomach at the point when meat-digestion is poised to do its worst—nipping the problem in the bud, as it were.

Sudden infant death syndrome

The cradle, not the grave

Jul 3rd 2008
From The Economist print edition

A chance observation may help explain why some babies die unexpectedly

SUDDEN infant death syndrome (SIDS) is the biggest killer of babies over one month old in the rich world (many things kill babies who are younger than this). What SIDS actually is, though, is a mystery. By definition, the child is dead when the diagnosis is made. That means researchers usually have only post mortem data about the symptoms to go on.

Such data are not valueless, however. Some of the nerve cells of SIDS victims' brainstems often look strange. The cells in question regulate basic bodily functions, including breathing and body temperature, and in SIDS babies they are more numerous and less mature than they are in babies who have died of other causes.

These cells communicate using a messenger molecule called serotonin. That gives researchers a way in, and Enrica Audero and her colleagues at the European Molecular Biology Laboratory in Monterotondo, Italy, have now opened it. They have, as they report in this week's *Science*, discovered that mice which have been genetically engineered in a way that disturbs their serotonin metabolism also die early.

To start with, Dr Audero and her team were asking a completely different question—one about serotonin's role in aggression. However, they found this difficult to answer because their mice kept dropping dead. It was at that point they realised they might have stumbled upon an animal model of SIDS.

Their original experiment used a genetic switch to regulate production of a particular receptor molecule for serotonin. To make their SIDS model they tweaked this switch so that it came on when the mice were three weeks old (mice are born prematurely, relative to people, so that corresponds roughly with the moment of human birth) and then looked to see what would happen. In particular, they looked for symptoms that might lead to death.

What they found was that before the manipulated mice died, they suffered from brachycardia (abnormally slow heart rate) and hypothermia. At the moment, nobody knows if SIDS babies die of brachycardia or hypothermia or both. It is, however, a plausible hypothesis, and there is some evidence that their autonomic nervous systems (which control basic bodily functions such as heartbeat and body temperature) have not been working properly.

As so often, these findings raise as many questions as they answer. For one thing, SIDS is more than twice as common in boys as it is in girls. That sex bias is absent in the mice. Moreover, the changes seen in mouse brains are not exactly the same as those observed in SIDS babies, in whom the serotonin receptor in question, known as 1A, is, if anything, underactive. And a study published earlier this year, by Megan Morley of Rush University in Chicago, found no evidence of an association between abnormalities in the gene for the 1A receptor and a baby's risk of SIDS.

As regards the brain changes, a model is only a model—and in this case an accidental one. Better models may now be constructed. And the fact that no changes in the receptor gene itself were noticed by Dr Morley does not mean this gene is not involved. Dr Audero's experiment did not manipulate the receptor gene directly but, rather, manipulated its activity using the switch. The importance of such second-order genetic effects is only now being appreciated. But they are likely to explain many diseases that classical genetics cannot.

This experiment does, however, suggest that genetics alone may explain some cases of SIDS. In the past, explanations have concentrated on environmental factors such as the smoking habits of the parents, bacterial infection and (most famously) a baby's sleeping position. These are clearly involved in some cases, but have never looked satisfactory as complete explanations. Dr Audero's results suggest that some upset of the serotonin system may be a necessary, but not always sufficient, part of the pattern that leads to SIDS. It will be enough to kill some children, but needs an environmental "boost" in other cases.

If research can establish that is true, then it may be possible to screen infants and single out those at risk, so that parents can take suitable precautions. That would be a very good thing indeed.

The Phoenix Mars probe

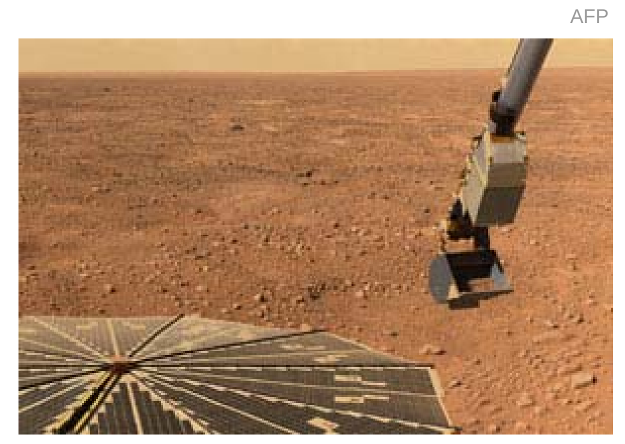
Up the garden path

Jul 3rd 2008
From The Economist print edition

The latest results in the search for Martians

“SPIT on the desert and a flower grows.” That, at least, is the proverb on Earth. On Mars, however, you might hope for asparagus, green beans and turnips if the latest results from *Phoenix* are to be believed. An analysis carried out by the probe, which landed on May 25th, suggests the local regolith (the crushed rock that passes for soil on Mars) is slightly alkaline—which such vegetables prefer. That is a surprise. The regolith was expected to be very acid—probably too acid even for crops such as peanuts, potatoes and carrots that like their soils with low pH.

AFP



Awaiting the plough

Of course, no one is really interested in what crops could grow in it. If people ever do live on Mars they will rely on hydroponic farms for food. The actual question that hangs over every result from Mars is “what does it say about the chances of there being Martians?”

Well, this one confirms—yet again—that there was once liquid water on Mars. The components of various common salts (magnesium, sodium, potassium and chloride ions, in particular) turned up in quantity. On Earth, such salts are the result of the chemical action of water on volcanic minerals, so it is reasonable to assume the same is true on Mars.

Phoenix has suggested, too, that water in solid form is still present. On June 15th its digging arm turned up several dice-sized clumps of bright material. These might have been either ice or salt, but they vanished over the course of four days, which strongly implies they were ice and had evaporated.

Absolute confirmation of this must wait a few days. The regolith was analysed by a chemistry set known as the Microscopy, Electrochemistry and Conductivity Analyser, which contains so much water itself that it cannot detect the stuff in samples. That is the job of the Thermal and Evolved-Gas Analyser, which has just been loaded up with a sample of its own and will report in due course. More disappointingly for eager exobiologists, there has been no sign so far of the sorts of organic compounds that might be part of (or have once been part of) living things.

Family history

Mount Lebanon's children

Jul 3rd 2008
From The Economist print edition

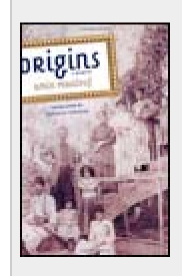
Bridgeman Art Library



A fine family memoir explores notions of emigration, identity and sectarianism

"ELDERLY persons are a treasure we squander in cajoleries and blandishments," laments Amin Maalouf as he explores the history of his Lebanese family without the benefit of the memories of the old aunts and cousins he had never thought to interrogate until it was too late. The unearthing of a great trunk of documents belonging to his grandfather, Botros, an eccentric poet, orator and teacher who lived on Mount Lebanon at the turn of the 19th century, sets him off on his journey of discovery in an attempt, among other things, to understand why some of his family left their villages—for America, Egypt, the Gulf—while others stayed on.

Origins: A Memoir.
By Amin Maalouf
By Translated by Catherine Temerson



Farrar, Straus and Giroux; 404 pages; $26. To be published in Britain by Picador in September

In particular he is intrigued by the family legend that in 1902 Botros undertook a mission to Cuba to rescue his brother, Gebrayel, who had migrated there in 1895 and was said to be in dire legal and financial trouble. Botros learnt Spanish on his 40-day outward journey and returned home triumphant, mission accomplished. Mr Maalouf, whose detective work takes him on many a gentle adventure in modern-day Havana, discovers the legend to be largely a fabrication. Gebrayel, far from being in distress, had prospered as a respected Havana shopkeeper. He had tried to persuade his brother to join him and Botros, half-tempted, gave emigration a go. But it didn't work out and he returned disillusioned to the mountains.

This little tale allows Mr Maalouf to reflect on the complex problems of identity that beset minorities such as his own Christian Lebanese family. Botros and Gebrayel, who lived through the dying years of the Ottoman Empire in the province of Syria, were described as being of Turkish nationality or Syrian race as they passed through Ellis Island on their journeys to or from Cuba. Mr Maalouf himself spoke Arabic and English as a young boy but, much later, was forced into exile by Lebanon's civil war. He now lives in Paris, writing in French. Many of the characters in his novels, including "The Rock of Tanios" which in 1993 won France's Prix Goncourt, are wanderers among lands, languages and religions, finding themselves poised between distinct cultural traditions.

There are no Muslims in “Origins” but the sharpness of the clashes within Christian Lebanon—Maronites, Greek Orthodox, Greek Catholics, Protestants—foreshadows sectarian trouble. Through marriage and schooling (American Protestant mission schools creating converts), the Maalouf family was thoroughly mixed up, and mostly was happy with this. But on both the Catholic and the (smaller) Protestant sides there were fierce fundamentalists who allowed for no compromise.

Botros was not one of those. A larger-than-life character of ideals, whims and rages, he defied the conventions of the time, refusing to allow his children to be baptised (so that they could later choose their own denomination) and giving a daughter an Arabicised boys’ name, Kamal, out of his respect for Turkey’s secular leader, Kemal Ataturk. Startling for the time and place, the Universal School, which he and his wife, Nazeera, started in one room of their small house, was both secular and co-educational. Botros fought a bitter war with the much more traditional Catholic school across the way, sometimes winning battles. But the French, when they took over the new state of Lebanon after the first world war, favoured the priests and their school.

Botros was a rebel, though within limits: he thought the collapsing Ottoman empire could be saved as a constitutional monarchy, a state composed of many nations. He saw himself as a pioneer, ramming home his ideas about “restructuring the Orient” in speeches and plays. In one of these he has a fellow-Lebanese remark: “We constantly wear two faces; one to ape our ancestors, the other to ape the West”.

He also wrote verse for every great occasion, some of it pretty awful, such as a poem addressed to the Mail Service of the Orient after it had brought him news of Gebrayel’s death in a car accident in 1918. Mr Maalouf is a bit relentless in quoting poems, letters and official documents at considerably greater length than most readers can willingly digest. His expectation of a continuing interest in the minutiae of his genealogical research is high. But the splendid picture of his grandfather, in a perpetual state of rage, bare of head with a black cape which “fluttered behind him like a pair of wings”, as he quixotically attacks the prejudice all around him, is worth a mild sigh or two.

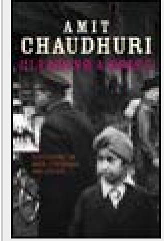
Origins: A Memoir. By Amin Maalouf.
Translated by Catherine Temerson.
Farrar, Straus and Giroux; 404 pages; $26. To be published in Britain by Picador in September

India and its literature

Back to modernity

Jul 3rd 2008
From The Economist print edition

Clearing a Space: Reflections on India, Literature and Culture
By Amit Chaudhuri



Peter Lang; 330 pages; £12.99

IT MAKES a change, amid the global excitement over India's economic rise and the tremendous military, diplomatic and commercial influence that will follow it, to encounter an elegiac Indian. Rarer still, Amit Chaudhuri's elegy is not for Mahatma Gandhi's agrarian Utopia—the commonest fantasy of Indian dissidents. Rather, it is for a kind of Indian literature and literary sensibility, which he reveres, and now is scarce.

Written over a 15-year period, in which he has excelled as a novelist and academic, Mr Chaudhuri's essays elucidate an Indian modernist tradition, which he finds rooted in 19th-century Bengali humanism and is characterised by "ellipsis and disjunction". India's most celebrated modern poet, Rabindranath Tagore, a Bengali like Mr Chaudhuri, whom he explains beautifully, offers lyrical examples of this. But bringing them to view—or "clearing a space"—is heavy work. It involves pruning back two choking analyses of modern Indian literature: the post-colonial and post-modern.

AFP

The constant gardener

On the first task, Mr Chaudhuri makes skilful use of his secateurs. He finds plenty of tension in modern Indian fiction; but not all of it is, as post-colonialists might suppose, in response to empire. In fact, the struggle of Indian writers, like writers everywhere, is mostly within themselves. But the second thorny hedge proves impossible to clear. Post-modernism, writes Mr Chaudhuri, is "polyphony; the conflation and confusion of fantasy with history", a "rhetoric of excess, plenty and a relentless engulfing inclusiveness", which has been the context for Indian writers since the 1981 publication of Salman Rushdie's babbling narrative, "Midnight's Children".

An exhausting theorist, Mr Chaudhuri (pictured above) likens this and the Indian literature that has followed it—with all its variety and interconnectedness—to globalisation. Literary merit, he says, has become synonymous with commercial value; "today's writers are stocks and shares". Here, the poet in Mr Chaudhuri asserts himself: "The triumphal narrative of Indian writing"—perhaps even including Mr Rushdie's feted trickery—"bores me, personally speaking, as a reader and writer."

This tension between Mr Chaudhuri's intellect and aesthetic, between the theorist and the artist, is engaging. It rewards a second reading of his essays, which is a blessing, because at first look many passages are impenetrable. Mr Chaudhuri's quest for precision, expressed in endless sentences, linking clause upon qualifying clause, may be admirable. But his taste for ugly terminology ("ironicises", "problematises") is a turn-off. Irksome, too, are the places where Mr Chaudhuri's theorising rambles far from the text where it began. A short essay on the imagination of Ashis Nandy, a cultural theorist, for example, has virtually nothing on Mr Nandy's views.

Elsewhere, Mr Chaudhuri is more helpful. He explains India's unique understanding of the word "secular": a national tolerance of diverse religions, as prescribed by the country's constitution. He describes, respectfully, the dramatic uses that Indian poets have made of humdrum English words—rescuing them from Mr Rushdie's mocking description of this, "chutnification". Like Amartya Sen before him, Mr Chaudhuri also excoriates India's Hindu nationalists, whose taproot he sees in European fascism, not

ancient beliefs.

There are light moments too, especially in Mr Chaudhuri's memories of his childhood in Calcutta and Bombay: a city that "keeps inventing and reinventing itself, bruising itself as it looks for acceptance". There are also jokes, like Yeats responding to Tagore much as "business executives are reported to respond to Paul Coelho".

And, finally, there is a joke that Mr Chaudhuri, though he forces a grin, doesn't find funny. It is Bollywood, the film industry which has become a powerful emblem of India's emergence despite turning out endless moronic parodies. Pausing briefly, Mr Chaudhuri, the earnest poet, dismisses any possibility of Bollywood containing "artistic value". And then the critic recollects himself, and Mr Chaudhuri reflects that, "of course", the idea of artistic value is meaningless these days.

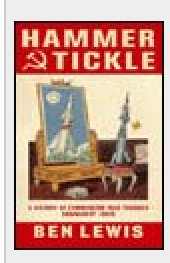
Clearing a Space: Reflections on India, Literature and Culture.
By Amit Chaudhuri.
Peter Lang; 330 pages; £12.99

Communist jokes

Funny bones

Jul 3rd 2008
From The Economist print edition

Hammer & Tickle: A History of Communism Told Through Communist Jokes
By Ben Lewis



Weidenfeld & Nicolson; 354 pages; £14.99

Buy it at
Amazon.com
Amazon.co.uk

JOKES under communism were not just a welcome contrast to the dreariness of everyday life; they also helped undermine it. For example. "How do you deal with mice in the Kremlin?" "Put up a sign saying 'collective farm'. Then half the mice will starve and the others will run away."

Ben Lewis has collated some of the best, and best-known, jokes that were told under more than seven decades of communist rule. His work is based on more than 40 previously published collections ranging from underground selections, to those published by anti-communist émigrés, and a large sprinkling that appeared after 1989, once it was safe to air them.

Most make you giggle and groan in equal measure. It is worth remembering that in some countries and some eras, being overheard telling or laughing at just one of these jokes could mean you died in a labour camp; there are plenty of jokes about that too. "Who built the White Sea canal [Stalin's single most murderous slave-labour project]?" "The left bank was built by those who told the jokes, and the right bank by those who listened."

But the aim of "Hammer & Tickle" is not just to be amusing and poignant, but also to instruct. The author makes the (to him) rather depressing discovery that most communist-era jokes were just recycled versions of older ones. Take this example, which is told twice in the book: a flock of sheep approaches the Finnish border in a panic, pleading to be allowed entry. "Beria [Stalin's secret police chief] has ordered the arrest of all elephants," they explain. "But you're not elephants," reply the Finnish border guards in puzzlement. "Yes, but try explaining that to Beria." That sounds spot-on for the Soviet Union in the 1930s. But it can be traced to a Persian poet in 12th-century Arabia, where it involves a fox running away from a royal ordinance that in theory applies only to donkeys.

Unfortunately, Mr Lewis is not content to laugh and remember. He wants a "serious comparative study" of the subject. It is tempting to think that he is joking, and that his theoretical elaborations about the true significance of communist-era jokes are a subtle parody of the way that modern literary critics so often miss the point of the texts they write about. It is almost comical to read his po-faced but pointless consideration of whether jokes about Stalin predated Stalin's own jokes—almost comical, but not quite.

If Mr Lewis is indeed joking, he pushes it too far. The potted histories of communism he provides as context are leaden and sometimes sloppy. The travelogue of his meetings with jokesters across the Eastern block is fun at first but then becomes dull. In particular, the conceit of linking his research to the ups and downs of his relationship with a tiresomely pro-communist (and humourless) girlfriend from East Germany is jarringly intrusive and self-referential.

No matter: rather than worrying about whether humour was ultimately a safety-valve for communism or subversive of it, the reader can skip ruthlessly and concentrate on the jokes, and the remarks people have made about them. "Jokes against the Party constitute agitation against the Party," raged Matvei Shkiriatov, a zealous Stalinist, at a Central Committee Meeting in January 1933. That was echoed by Hitler's propaganda chief, Josef Goebbels, in 1939, when he wrote: "We will eradicate the political joke." But they didn't.

Many of the jokes told about past Soviet leaders are now told about Vladimir Putin (Stalin appears to him in a dream and says: "I have two bits of advice for you: kill your opponents and paint the Kremlin blue." Putin asks, "Why blue?"). The world would be a poorer place without the jokes sparked by ridiculous yet ruthless rulers. But Russia would be a lot happier.

Hammer & Tickle: A History of Communism Told Through Communist Jokes.
By Ben Lewis.
Weidenfeld & Nicolson; 354 pages; £14.99

Amazon worldwide bestsellers

Fearless

Jul 3rd 2008
From The Economist print edition

James Bond and Stephanie Plum vie to be the most popular crime heroes

STEPHANIE PLUM, the heroine of “Fearless Fourteen”, measures five feet, seven inches. Her hair is brown and naturally curly. Her eyes are blue, her teeth mostly straight and three days ago her manicure was pretty good. Her long-time boyfriend is called Morelli and they drive each other mad.

Ms Plum would like to be a domestic goddess; instead she is a bond-enforcement agent working for her cousin Vinnie. Her creator, Janet Evanovich, has given her more luck than talent, though you would not necessarily know that from the opening page of the book, the 14th in the series, which starts with a bank robbery that goes wrong.

James Bond may like to leave his enemies shaken *and* stirred and Jack Reacher to take them on six at a time. Neither is a match, though, for Ms Plum, who last month outsold all the boys and became the world’s biggest selling crime hero. Don’t mess with this woman.

Crime’s most wanted

1. Fearless Fourteen
by Janet Evanovich

Click to buy from Amazon.com or Amazon.co.uk

2. Sail
by James Patterson

Click to buy from Amazon.com or Amazon.co.uk

3. Devil May Care
by Sebastian Faulks

Click to buy from Amazon.com or Amazon.co.uk

4. The Pillars of the Earth
by Ken Follett

Click to buy from Amazon.com or Amazon.co.uk

5. Bockmist (“The Gunseller”)
by Hugh Laurie

Click to buy from Amazon.com or Amazon.co.uk

6. Nothing to Lose
by Lee Child

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7. Plague Ship
by Clive Cussler

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8. World Without End
by Ken Follett

Click to buy from Amazon.com or Amazon.co.uk

9. No Time For Goodbye
by Linwood Barclay

Click to buy from Amazon.com or Amazon.co.uk

10. Odd Hours
by Dean Koontz

Click to buy from Amazon.com or Amazon.co.uk

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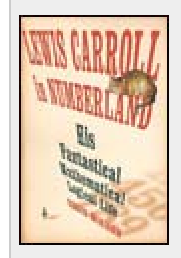
Lewis Carroll

Shoes and ships and sealing wax

Jul 3rd 2008
From The Economist print edition

THE immortal whimsy of the Alice books are Lewis Carroll's claim to fame. The Queen of Hearts, the Mad Hatter, the Cheshire Cat and other products of Carroll's curiouser and curiouser brain are pre-eminent gods in the pantheon of absurdity. Historians of photography remember Carroll too, for his pioneering portraits of children and eminent Victorians. But the Reverend Charles Dodgson—to give Carroll his real name—failed to make a mark in his day-job as a mathematician.

Lewis Carroll in Numberland: His Fantastical Mathematical Logical Life
By Robin Wilson



To be published in America by Norton in November Allen Lane; 256 pages; £20.

Like his father before him, Dodgson taught mathematics at Christ Church, Oxford. His professional writings were as playful and eccentric as his light verse and stories, which may be one reason why he is at most a footnote in the history of mathematics. In this little book, Robin Wilson, whose father, Harold, was Britain's prime minister, aims to give an elementary treatment of Dodgson's mathematical work for the general reader.

Mr Wilson's account is set in the context of Dodgson's life and traces the evolution of his interests, which was relatively slight. Dodgson's transition from a childhood with three brothers and seven sisters in a secluded Cheshire parsonage to adulthood—if that is the word—in the cloisters of Christ Church, where he lived from the age of 18 until his death, was a barely noticeable change. The House, as Christ Church is known, became a larger version of his childhood home. The Alice for whom his best-known books were written was a daughter of the House's patriarch, Dean Henry Liddell.

The gently didactic tone of many of Dodgson's mathematical works echoes not only the Alice books but also the pieces he composed for his siblings as a child, and the letters he wrote to them from Oxford as a student. The mathematics was like the man: conservative and provincial. Dodgson could be passionate when defending old ways of teaching Euclid, but not about much else. And he was prodigiously gifted at concocting puzzles. The mathematics in this book is not hard, but neither is it very interesting, unless you are an algebra nerd.

One small part of Dodgson's work, though, has impressed social scientists: his analysis of the mathematics of voting. His interest in the topic was sparked by the deliberations of his colleagues at Christ Church over such matters as how to choose a new belfry. Dodgson's pamphlets on voting were largely ignored until 1958, when a British economist, Duncan Black, noticed that there had been nothing so good on the topic since just after the French Revolution.

In 1984, an Oxford professor of logic, Michael Dummett, rued the fact that Dodgson had never completed a planned book on voting, and averred that "it seems possible that, had he ever published it, the political history of Britain would have been significantly different." Mr Wilson quotes this surprising remark, which neither he nor Mr Dummett explains. Presumably they mean that Dodgson's advocacy might have persuaded Britain to adopt a form of proportional representation, in which case the author's father might never have become prime minister.

Towards the end, Dodgson focused on symbolic logic. His work was old-fashioned by the standards of the day, though rich with ingeniously bizarre examples. Perhaps his most gloriously pointless project was the "Game of Logic", a board-game with coloured counters that was meant to develop children's powers of logical thought by getting them to mess about with Aristotelian syllogisms. It is no match for "Alice's Adventures in Wonderland" and "Through the Looking-Glass". Dodgson was more successful at getting people to entertain silly thoughts than he was at getting children to think logical ones.

Lewis Carroll in Numberland: His Fantastical Mathematical Logical Life.

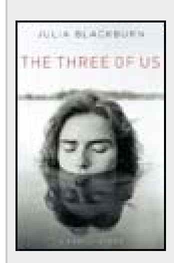
By Robin Wilson.
Allen Lane; 256 pages; £20.
To be published in America by Norton in November

Family stories

They mess you up

Jul 3rd 2008
From The Economist print edition

The Three of Us: A Family Story
By Julia Blackburn



Pantheon; 313 pages; $26.
Jonathan Cape; £16.99

Buy it at
Amazon.com
Amazon.co.uk

WHEN Julia Blackburn screamed as a child it was because her parents spoke about her as though she wasn't there. It was an assertion of selfhood. When she screamed as a young woman it was "like disembowelling myself", an annihilation of selfhood. It is a wonder these memoirs ever got written. You tremble for the author as she unfolds the chaos of her family, tracing it back through parents and grandparents to its poisoned origins in the sexual repression, racism, violent religion, snobbery and war of the 19th and early 20th centuries.

Ms Blackburn's route into these depths is surprisingly direct. As readers will recall, in her first novel, a thinly fictionalised memoir entitled "The Book of Colour" which was published in 1995, her great-grandfather was a missionary whose job was "to stamp out copulation" among the "natives" of an Indian Ocean island. Far from doing that, he married one himself, producing a dark-skinned son who in turn became a vicar so obsessed with colour and sex that he fitted his own son (Ms Blackburn's father, Thomas Blackburn, a poet) with a metal contraption to repress wet dreams, and washed the boy's face in bleach and lemon.

On Ms Blackburn's mother's side it was money, snobbery, sexism and war. A very rich great-grandmother disinherited her daughter for marrying the "wrong" man. In 1914 the couple had an adored daughter whom they treated as a boy. After the father returned, broken, from 15 months in the trenches, a second daughter was born (Ms Blackburn's mother, Rosalie de Meric, a painter), whom they did not adore and treated as a girl. The marriage died, and the sisters were taught to fight each other, scratching and hitting. Their father shouted encouragement to the eldest, and cuddled up in bed with her at night. Later, the favoured sister committed suicide.

By a trick of fate and psychology, Thomas and Rosalie—intelligent, creative, and haunted—found each other. Their marriage developed into a little hell, and their daughter Julia, the author of this memoir which came out in Britain in May and is published in America this month, grew up against a soundtrack of murderous rows and breaking glass. Her father became an alcoholic, addicted to prescriptive drugs, chronically adulterous and so violent that divorce was inevitable. Her mother then took in lodgers through whom she set herself up in sexual competition with her then teenage daughter—a game of triangles that she eventually lost.

This is a terrible and moving memoir, both raw and artful. The "muddle and sadness and fight of it all" is refracted through the careful telling, the choice of detail, the remembered voices and the cunning weave of past with present. As Ms Blackburn writes, her mother is dying, and in a series of forward flashes the reader watches the two of them, in the nick of time, bury the past and find love. And the daughter? It had been a close shave, but what saved her in the end came from her father at his best: a love of writing, language, learning poetry, telling stories, singing songs—a soundtrack of her own, louder than breaking glass.

The Three of Us: A Family Story.
By Julia Blackburn.
Pantheon; 313 pages; $26.
Jonathan Cape; £16.99

19th-century Scandinavian art

The lightness of being

Jul 3rd 2008
From The Economist print edition

The mysterious paintings of Vilhelm Hammershoi

VILHELM HAMMERSHOI has been a well-kept secret since his death in 1916. All his best-known paintings are of household interiors that are drained of colour and tell no stories. His windows cannot be seen through, his doors cannot be opened and the figures produce no element of vitality into the rooms. Hammershoi is defiantly inscrutable; the mood is melancholic and enigmatic, but the paintings are oddly compelling. Quite why, no one seems sure.

Royal Academy of Arts



Let there be light

Of the 71 paintings in a new exhibition in London, 21 come from his native Copenhagen, 15 from other Scandinavian collections and 20 from private collections, principally Danish. Hammershoi's focus was not as narrow as this show might suggest, but to see his nudes it is necessary to visit the Statens Museum for Kunst in Denmark. He did some fine, if bleak, landscapes too, but it was the interiors that sold in his lifetime, and he is best remembered for paintings of the sun shining through curtainless window-panes, casting shadows on carpetless floors. Anxious to transform the prosaic into the romantic, his admirers speak of a poet of light and the poetry of silence.

Hammershoi himself was guileless. “What makes me choose a motif are the lines, what I like to call the architectural context of an image,” he said in 1907. Light was also very important, but it was lines, he insisted, that had the greatest significance for him. His wife, Ida, makes appearances in the empty rooms, but she is usually painted from the back, with the emphasis on the bare nape of her neck. The heroic figures are white doors and windows, and tables, chairs, a piano and a sofa. No painter can have got so much pleasure from painting brown furniture. One work, titled “Interior with a Woman at a Sewing Table”, is a symphony of three shades of shiny brown.

Hammershoi was influenced by Vermeer and the 17th-century Dutch genre painters and by Caspar David Friedrich, a German, but there is no one like him. His work shows traces of an unexpected subversive sense of humour. Felix Krämer, the show's curator, identifies irregularities, for example, that create an almost surreal quality: a piano with two legs, table legs casting shadows in different directions, chests of drawers with no knobs or handles. Even some of Hammershoi's admirers wonder what it all means.

Trying to pin Hammershoi down is as profitless as waiting for Godot. However, the new exhibition at the Royal Academy of Arts might encourage some excitement in the marketplace. The highest price made by a Hammershoi interior is £520,000 ($1m) in 2006 and the price boom in the auction houses is passing him by. Perhaps the secret of Hammershoi has been kept a bit too well.

“Vilhem Hammershoi: The Poetry of Silence” is at the Royal Academy of Arts, London, until September 7th. It will then travel to the National Museum of Western Art in Tokyo from September 30th to December 7th

Sam Manekshaw

Jul 3rd 2008
From The Economist print edition

EPA



Sam Manekshaw, soldier, died on June 27th, aged 94

HIS most famous remark was not, strictly speaking, true. On the eve of the war with Pakistan in December 1971 that led to the creation of Bangladesh, India's prime minister, Indira Gandhi, asked her army chief, Sam Hormusji Framji Jamshedji Manekshaw, if he was ready for the fight. He replied with the gallantry, flirtatiousness and sheer cheek for which he was famous: "I am always ready, sweetie." (He said he could not bring himself to call Mrs Gandhi "Madame", because it reminded him of a bawdy-house.)

Yet General Manekshaw himself recounted a cabinet meeting in Mrs Gandhi's office in April 1971. To forestall secession, the Pakistani government had already cracked down in what was then East Pakistan. Hundreds of thousands of refugees had crossed the border into India. Mrs Gandhi wanted the army to invade Pakistan. General Manekshaw resisted. The monsoon, he pointed out, would soon start in East Pakistan, turning rivers into oceans. His armoured division and two infantry divisions were deployed elsewhere. To shift them would need the entire railway network, so the grain harvest could not be transported and would rot, bringing famine. And of his armoured division's 189 tanks, only 11 were fit to fight.

He was not, in other words, ready. But, as he put it, "There is a very thin line between being dismissed and becoming a field-marshal." Mrs Gandhi rejected the resignation he offered, and acceded to the delay he wanted. His job, he told her, was to fight to win. In December he did, cutting through the Pakistani army like a knife through butter, and taking Dhaka within two weeks. Quibblers later noted that this was not one of his original war aims. He had the most important attribute of any successful general: good luck.

That was not the only time he threatened to quit. Mrs Gandhi once questioned him about rumours that he was plotting a coup. In response, he asked if she wanted his resignation on grounds of mental instability. Yet if she and other politicians were in awe of him as a professional soldier and grateful for his lack of political ambition, his men loved him for his willingness to take on their civilian bosses and stand up for the army's interests.

He had shown this in the Indian army's darkest hour, the abject defeat in 1962 by China. Already a general, he had the previous year quarrelled with India's defence minister, V.K. Krishna Menon, about national security. He was vindicated when the Chinese army swatted aside Indian resistance and briefly

occupied what is now the state of Arunachal Pradesh. Mr Menon resigned. General Manekshaw was rushed to the front to rally the demoralised troops. His first order was: “There will be no withdrawal without written orders and these orders shall never be issued.”

General Manekshaw was able to demand courage from his soldiers because his own was not in doubt. Known as Sam “Bahadur”, or Sam the Brave, an honorific given him by the Indian army’s Gurkhas, the first of his five wars was for the British in Burma, where he was seriously wounded. Assuming he would die, an English general pinned his own Military Cross on Captain Manekshaw’s chest, since the medal could not be awarded posthumously. Another story has it that a surgeon was going to give up on his bullet-riddled body, until he asked him what had happened and got the reply, “I was kicked by a donkey.” A joker at such a time, the surgeon reckoned, had a chance.

Stiff but hairy

There was something of British military tradition in his stiff upper lip, the lavish handlebar moustache in which he cloaked it, the dapper little embellishments to his uniform and his partiality for Scotch whisky. Yet he was born into a very particular and tight-knit community: India’ s small and dwindling Parsi minority, which has produced a disproportionate number of leading Indians, such as the members of the Tata and Godrej business dynasties. Sam Manekshaw was another Parsi overachiever. He was the first of only two field-marshals ever created in the army.

Yet his retirement since 1973 was not one long bask in glory. Former deputies felt he had monopolised the credit for various victories. Then last year his name was linked to bizarre allegations, by the son of a former Pakistani president, against an unnamed brigadier who had once sold Indian war plans to Pakistan. All nonsense, said those who knew him. Already in hospital, General Manekshaw was in part shielded from controversy.

After his death, anger at the slur, and at the lack of proper honour for one of India’s true heroes, rumbled on. The prime minister, along with the army, navy, and air-force chiefs, all missed his funeral—which was a modest one held in Tamil Nadu in the south, not a grand one in the capital. His friends grumbled that even foreigners such as Lord Mountbatten were afforded greater respect in death. Bangladesh, however, paid grateful tribute to his part in the nation’s foundation.

He too might well have been disappointed that his obsequies were not grander. His last words were “I’m OK”, though he had rehearsed a better line nearly 37 years earlier. For death at least, the brave soldier had indeed shown himself “always ready”.



Overview

Jul 3rd 2008
From The Economist print edition

Consumer-price inflation in the **euro area** rose to 4% in June, according to a provisional estimate, well adrift of the central bank's target ceiling of 2%. The euro zone's unemployment rate was stable, at 7.2% in May. The jobless rate in **France** edged down to 7.4%; in **Spain** it rose from 9.6% to 9.9%. **Ireland's** GDP fell by 1.5% in the year to the first quarter.

American manufacturing perked up in June, according to the Institute for Supply Management. Its index rose from 49.6 to 50.2.

Britain's housing bust is deepening. The number of mortgages approved for house purchase plunged to 42,000 in May, below the nadir of the early 1990s and a 64% drop from May 2007. House prices fell for the eighth month in a row in June, according to Nationwide, a mortgage lender, leaving them 6.3% lower than a year earlier. Meanwhile, the June survey of purchasing managers revealed that activity in British manufacturing was at its weakest since December 2001.

Turkey's GDP rose by 6.6% in the year to first quarter, stronger than most forecasts.

Australia's central bank left its benchmark interest rate unchanged, at 7.25%, at its meeting on July 1st.

Business confidence in **Japan** is still ebbing, according the central bank's quarterly Tankan survey. The percentage balance of large manufacturers reporting "favourable" over "unfavourable" conditions fell from 11 in March to five in June, nearly a five-year low.



Output, prices and jobs

Jul 3rd 2008
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2008†	2009†	latest	latest	year ago	2008†	rate‡, %
United States	+2.5 Q1	+0.9	+1.4	+1.3	-0.1 Apr	+4.2 May	+2.7	+4.2	5.5 May
Japan	+1.3 Q1	+4.0	+1.4	+1.3	+1.2 May	+1.3 May	nil	+1.4	4.0 May
China	+10.6 Q1	na	+9.8	+9.0	+16.0 May	+7.7 May	+3.4	+6.5	9.5 2007
Britain	+2.5 Q1	+1.1	+1.6	+1.2	+0.2 Apr	+3.3 May§	+2.5	+3.4	5.3 Apr††
Canada	+1.7 Q1	-0.3	+1.3	+2.0	-4.5 Apr	+2.2 May	+2.2	+2.0	6.1 May
Euro area	+2.2 Q1	+3.2	+1.7	+1.3	+3.9 Apr	+4.0 Jun	+1.9	+3.5	7.2 May
Austria	+3.5 Q1	+3.2	+2.3	+1.9	+3.0 Apr	+3.7 May	+2.0	+3.0	4.1 May
Belgium	+2.2 Q1	+1.9	+1.7	+1.5	-1.3 Mar	+5.8 Jun	+1.3	+3.9	9.9 May‡‡
France	+2.2 Q1	+2.6	+1.7	+1.3	+3.2 Apr	+3.3 May	+1.1	+3.2	7.4 May§§
Germany	+1.8 Q1	+6.1	+2.0	+1.5	+4.8 Apr	+3.3 Jun	+1.9	+2.9	7.8 Jun
Greece	+3.6 Q1	+4.5	+2.9	+3.0	+2.0 Apr	+4.9 May	+2.6	+4.2	9.0 Mar
Italy	+0.3 Q1	+1.9	+0.4	+0.8	+2.0 Apr	+3.8 Jun	+1.7	+3.4	6.5 Q1
Netherlands	+3.3 Q1	+1.8	+2.4	+1.7	+0.4 Apr	+2.6 Jun	+1.7	+2.4	4.0 May††
Spain	+2.7 Q1	+1.2	+1.7	+1.2	+11.3 Apr	+4.6 May	+2.3	+4.2	9.9 May
Czech Republic	+5.3 Q1	+3.6	+4.7	+5.4	+12.2 Apr	+6.8 May	+2.4	+6.4	5.0 May
Denmark	-0.7 Q1	-2.4	+1.3	+1.4	+7.8 Apr	+3.4 May	+1.8	+3.1	1.7 May
Hungary	+1.7 Q1	+1.3	+2.0	+3.4	+6.7 Apr	+7.0 May	+8.5	+6.3	7.7 May††
Norway	+0.9 Q1	+0.8	+2.7	+2.4	-4.4 Apr	+3.1 May	+0.3	+3.4	2.5 Apr***
Poland	+6.1 Q1	na	+5.4	+4.3	+2.3 May	+4.4 May	+2.3	+4.2	10.0 May‡‡
Russia	+8.5 Q1	na	+7.2	+6.4	+6.7 May	+15.1 May	+7.8	+13.5	6.4 May‡‡
Sweden	+2.2 Q1	+1.6	+2.1	+2.0	+0.2 Apr	+4.0 May	+1.7	+3.3	5.9 May‡‡
Switzerland	+3.1 Q1	+1.3	+2.0	+1.5	+4.4 Q1	+2.9 Jun	+0.6	+2.4	2.4 May
Turkey	+6.6 Q1	na	+3.1	+4.0	+6.3 Apr	+10.7 May	+9.2	+10.5	11.6 Q1‡‡
Australia	+3.6 Q1	+2.5	+2.9	+2.8	+0.1 Q4	+4.2 Q1	+2.4	+3.7	4.3 May
Hong Kong	+6.8 Q1	+7.4	+4.8	+4.9	-4.4 Q1	+5.7 May	+1.3	+5.3	3.3 May††
India	+8.8 Q1	na	+7.7	+7.1	+7.0 Apr	+7.8 Apr	+6.7	+6.9	7.2 2007
Indonesia	+6.3 Q1	na	+5.9	+5.7	+2.6 Apr	+11.0 Jun	+5.8	+9.9	9.1 Dec
Malaysia	+7.1 Q1	na	+5.8	+5.7	+4.3 Apr	+3.8 May	+1.4	+5.2	3.0 Q4
Pakistan	+7.0 2007**	na	+3.6	+4.4	+4.3 Apr	+19.3 May	+7.4	+15.6	6.2 2006
Singapore	+6.7 Q1	+14.6	+4.5	+5.0	-12.8 May	+7.5 May	+1.0	+4.3	2.0 Q1
South Korea	+5.8 Q1	+3.3	+4.5	+4.3	+8.3 May	+5.5 Jun	+2.5	+3.5	3.2 May
Taiwan	+6.1 Q1	na	+4.3	+4.4	+5.3 May	+3.7 May	nil	+3.1	3.9 May
Thailand	+6.0 Q1	+5.9	+4.8	+4.7	+10.5 May	+8.9 Jun	+1.9	+7.2	1.5 Apr
Argentina	+8.4 Q1	+2.4	+6.0	+4.0	+8.6 Apr	+9.1 May	+8.8	+9.9	8.4 Q1‡‡
Brazil	+5.8 Q1	+2.9	+4.6	+3.6	+2.4 May	+5.6 May	+3.2	+5.7	7.9 May‡‡
Chile	+3.0 Q1	+5.8	+3.6	+3.8	-2.4 May	+8.9 May	+2.9	+7.5	8.0 May††‡‡
Colombia	+8.1 Q4	+6.8	+4.8	+4.3	+9.8 Apr	+7.2 Jun	+6.0	+6.5	11.0 Apr‡‡
Mexico	+2.6 Q1	+2.1	+2.3	+2.5	+5.5 Apr	+4.9 May	+3.9	+4.7	3.2 May‡‡
Venezuela	+4.8 Q1	na	+5.2	+4.0	-7.9 Mar	+31.4 May	+19.6	+30.8	8.2 Q1‡‡
Egypt	+6.9 Q1	na	+6.9	+6.7	+7.5 2007**	+19.7 May	+10.0	+17.1	9.1 Q4‡‡
Israel	+5.2 Q1	+5.4	+3.9	+3.6	+14.1 Apr	+5.4 May	-1.3	+4.2	6.3 Q1
Saudi Arabia	+3.5 2007	na	+7.2	+6.7	na	+10.4 May	+3.0	+8.5	na
South Africa	+4.0 Q1	+2.1	+3.9	+4.4	+9.8 Apr	+11.7 May	+6.9	+8.2	23.0 Sep‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	+0.1 Q1	+7.8	-0.6	+2.0	-6.7 May	+11.3 May	+5.7	+10.0	4.1 Apr
Finland	+3.1 Q1	+2.8	+2.8	+2.3	+4.2 May	+4.2 May	+2.4	+3.7	6.3 May
Iceland	+1.1 Q1	-14.0	+0.9	+1.7	+0.4 2007	+12.7 Jun	+4.0	+10.0	1.0 May‡‡
Ireland	-1.5 Q1	-0.9	+1.4	+1.5	-0.9 Apr	+4.7 May	+5.0	+3.6	5.4 May
Latvia	+3.3 Q1	na	+2.4	+2.6	+3.7 Apr	+17.9 May	+8.2	+15.0	5.1 Apr
Lithuania	+6.9 Q1	-0.8	+5.6	+5.0	na	+12.0 May	+4.8	+10.2	4.5 Apr‡‡
Luxembourg	+3.8 Q4	+7.4	+3.1	+3.0	+8.8 Apr	+4.0 May	+1.9	+3.6	4.1 May‡‡
New Zealand	+2.8 Q4	+3.1	+1.4	+2.3	+4.2 Q4	+3.4 Q1	+2.5	+3.3	3.6 Q1
Peru	+6.6 Apr	na	+7.5	+6.4	+16.5 Apr	+5.4 May	+0.9	+4.8	7.9 May‡‡
Philippines	+5.1 Q1	+3.0	+5.6	+5.7	-5.9 Mar	+9.6 May	+2.4	+6.8	8.0 April‡‡
Portugal	+0.9 Q1	-1.0	+1.5	+1.4	-6.4 May	+2.8 May	+2.4	+2.4	7.6 Q1‡‡
Slovakia	+8.7 Q1	na	+7.5	+5.2	+9.7 Apr	+4.6 May	+2.3	+4.0	7.4 May‡‡
Slovenia	+5.4 Q1	na	+4.5	+4.0	+6.9 Apr	+7.0 Jun	+3.6	+5.4	6.6 Apr‡‡

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions.- §RPI inflation rate 4.3% in May. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted.§§New series ***Centred 3-month average

The Economist commodity-price index

Jul 3rd 2008
From The Economist print edition

The Economist commodity-price index
2000=100

	Jun 24th	Jul 1st*	% change on one month	% change on one year
Dollar index				
All items	266.2	272.2	+8.6	+34.5
Food	272.2	280.6	+11.3	+66.2
Industrials				
All	258.3	261.3	+5.1	+6.4
Nfa†	206.4	207.1	+4.1	+30.1
Metals	286.8	291.0	+5.5	-0.6
Sterling index				
All items	204.8	207.3	+7.2	+36.2
Euro index				
All items	157.9	159.8	+6.6	+16.2
Gold				
$ per oz	890.00	942.90	+7.0	+44.4
West Texas Intermediate				
$ per barrel	137.09	141.42	+13.7	+98.0

*Provisional †Non-food agriculturals.

The Economist poll of forecasters, July averages

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The Economist poll of forecasters, July averages (previous month's, if changed)

	Real GDP, % change: Low/high range		Real GDP, % change: average		Consumer prices % increase		Current account % of GDP	
	2008	2009	2008	2009	2008	2009	2008	2009
Australia	2.5/3.6	2.5/3.8	2.9	2.8 (3.0)	3.7 (3.6)	3.0 (2.9)	-5.5 (-5.9)	-5.0 (-4.3)
Belgium	1.5/2.1	1.0/1.9	1.7	1.5 (1.7)	3.9 (3.0)	2.5 (2.1)	1.6 (2.1)	1.6 (2.0)
Britain	1.3/1.8	0.5/1.8	1.6 (1.7)	1.2 (1.4)	3.4 (3.0)	2.6 (2.4)	-4.1 (-3.9)	-3.8 (-3.2)
Canada	0.9/2.0	1.2/2.5	1.3 (1.4)	2.0 (2.1)	2.0 (1.8)	2.1	0.8 (0.2)	0.6 (-0.1)
France	1.5/1.8	0.9/1.8	1.7	1.3 (1.5)	3.2 (2.9)	2.2 (2.0)	-1.6	-1.6 (-1.7)
Germany	1.2/2.3	0.9/2.2	2.0 (1.9)	1.5 (1.6)	2.9 (2.7)	2.2 (2.0)	6.3 (6.1)	5.7 (5.5)
Italy	0.1/1.0	0.3/1.2	0.4 (0.6)	0.8 (1.1)	3.4 (2.9)	2.5 (2.1)	-2.6 (-2.5)	-2.5 (-2.4)
Japan	0.9/2.0	0.9/1.6	1.4 (1.3)	1.3 (1.4)	1.4 (1.1)	0.9 (0.8)	4.1 (4.3)	4.2
Netherlands	2.0/2.8	1.2/2.4	2.4 (2.6)	1.7 (2.0)	2.4 (2.3)	2.4 (2.3)	6.0	6.0 (6.2)
Spain	0.9/2.5	0.1/1.9	1.7 (2.1)	1.2 (1.8)	4.2 (3.8)	2.9 (2.7)	-9.5 (-9.1)	-8.5 (-8.4)
Sweden	1.8/2.6	1.3/2.6	2.1 (2.3)	2.0 (2.1)	3.3 (3.0)	2.5 (2.3)	8.1 (7.2)	7.6 (6.7)
Switzerland	1.5/2.3	1.1/2.0	2.0 (2.1)	1.5 (1.7)	2.4 (2.0)	1.7 (1.3)	15.1 (14.8)	14.5
United States	0.8/2.1	0.7/2.1	1.4 (1.2)	1.3 (1.5)	4.2 (3.8)	2.7 (2.6)	-4.9	-4.5
Euro area	1.5/1.9	1.0/1.7	1.7	1.3 (1.5)	3.5 (3.1)	2.4 (2.2)	-0.3 (-0.1)	-0.3 (-0.1)

Sources: ABN AMRO, BNP Paribas, Citigroup, Decision Economics, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, JPMorgan Chase, Morgan Stanley, Scotiabank, UBS



Trade, exchange rates, budget balances and interest rates

Jul 3rd 2008
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2008†	Currency units, per $ Jul 2nd	Currency units, per $ year ago	Budget balance % of GDP 2008†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−831.2 Apr	−710.7 Q1	−4.9	–	–	−2.4	2.13	3.96
Japan	+99.7 May	+213.5 Apr	+4.1	106	123	−2.9	0.75	1.66
China	+254.2 May	+371.8 2007	+9.8	6.85	7.59	0.3	4.49	4.56
Britain	−184.5 Apr	−102.4 Q1	−4.1	0.50	0.50	−3.6	5.91	5.13
Canada	+45.6 Apr	+14.5 Q1	+0.8	1.02	1.06	0.4	2.48	3.82
Euro area	+17.3 Apr	−2.5 Apr	−0.3	0.63	0.73	−0.9	4.96	4.65
Austria	+1.1 Mar	+14.8 Q1	+3.0	0.63	0.73	−0.4	4.96	4.84
Belgium	+12.3 Mar	−1.1 Mar	+1.6	0.63	0.73	−0.3	5.02	4.97
France	−61.6 Apr	−39.9 Apr	−1.6	0.63	0.73	−2.9	4.96	4.83
Germany	+278.6 Apr	+269.8 Apr	+6.3	0.63	0.73	1.1	4.96	4.65
Greece	−60.2 Mar	−46.4 Apr	−13.9	0.63	0.73	−2.6	4.96	5.25
Italy	−12.7 Apr	−57.8 Apr	−2.6	0.63	0.73	−2.6	4.96	5.24
Netherlands	+59.3 Apr	+50.7 Q1	+6.0	0.63	0.73	0.7	4.96	4.84
Spain	−149.4 Apr	−160.6 Apr	−9.5	0.63	0.73	−0.7	4.96	4.92
Czech Republic	+4.7 Apr	−3.6 Apr	−2.6	15.0	21.1	−2.2	4.23	5.16
Denmark	+4.2 Apr	+3.5 Apr	+0.9	4.70	5.46	3.8	5.60	4.96
Hungary	+0.5 Apr	−7.2 Q1	−5.9	149	180	−4.2	8.74	8.60
Norway	+70.7 May	+68.8 Q1	+17.5	5.07	5.83	17.8	6.55	5.08
Poland	−17.8 Apr	−19.9 Apr	−4.0	2.11	2.76	−2.0	6.67	6.69
Russia	+157.9 Apr	+92.4 Q1	+5.2	23.4	25.7	3.5	10.75	6.57
Sweden	+18.8 May	+40.4 Q1	+8.1	5.97	6.72	2.1	4.17	4.54
Switzerland	+14.6 May	+91.4 Q1	+15.1	1.02	1.22	0.9	2.79	3.26
Turkey	−69.7 May	−42.0 Apr	−6.5	1.24	1.29	−2.7	19.46	7.58‡
Australia	−21.3 May	−61.4 Q1	−5.5	1.04	1.16	1.6	7.76	6.57
Hong Kong	−26.0 May	+26.6 Q1	+9.3	7.80	7.81	3.0	2.30	3.44
India	−85.0 May	−17.5 Q1	−2.9	43.2	40.5	−3.2	8.71	9.43
Indonesia	+38.0 May	+10.9 Q1	+2.3	9,215	9,008	−1.8	9.41	7.82‡
Malaysia	+33.4 Apr	+30.6 Q1	+14.0	3.27	3.45	−3.1	3.69	4.52‡
Pakistan	−19.8 May	−10.5 Q1	−8.0	69.2	60.4	−6.2	13.88	11.90‡
Singapore	+29.6 May	+35.8 Q1	+23.3	1.36	1.52	1.0	1.19	3.30
South Korea	+1.5 Jun	+1.7 May	−0.8	1,037	920	1.1	5.36	6.02
Taiwan	+13.9 May	+32.2 Q1	+5.3	30.4	32.8	−1.9	2.75	2.64
Thailand	+7.9 May	+13.2 May	+0.4	33.4	34.2	−2.7	3.65	5.63
Argentina	+11.4 May	+7.9 Q1	+2.9	3.02	3.09	1.7	16.44	na
Brazil	+30.8 Jun	−15.2 May	−1.1	1.60	1.91	−1.6	12.17	6.16‡
Chile	+19.1 May	+4.3 Q1	−0.6	516	524	9.0	6.72	4.62‡
Colombia	+0.4 Mar	−5.0 Q1	−3.7	1,831	1,960	−1.6	9.80	6.08‡
Mexico	−8.9 May	−4.8 Q1	−1.1	10.4	10.8	nil	7.75	9.13
Venezuela	+30.1 Q1	+26.7 Q1	+10.6	3.45	4.23§	2.4	17.26	6.55‡
Egypt	−22.2 Q1	−0.1 Q1	+0.2	5.33	5.70	−7.1	10.08	5.48‡
Israel	−13.2 May	+4.4 Q1	+0.2	3.27	4.19	−1.3	3.88	5.56
Saudi Arabia	+150.8 2007	+95.0 2007	+34.6	3.75	3.75	21.0	3.64	na
South Africa	−11.0 May	−22.3 Q1	−8.0	7.82	6.97	0.4	12.50	10.75
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−4.3 Apr	−3.3 Apr	−10.5	9.86	11.5	−0.4	6.38	na
Finland	+12.3 Apr	+10.5 Apr	+4.7	0.63	0.73	4.5	4.89	4.82
Iceland	−1.4 May	−3.5 Q1	−13.5	78.1	62.0	1.0	15.82	na
Ireland	+37.2 Apr	−14.7 Q1	−3.2	0.63	0.73	−1.7	4.96	5.00
Latvia	−7.3 Apr	−6.2 Apr	−14.0	0.44	0.51	nil	5.84	na
Lithuania	−7.8 Apr	−5.8 Apr	−11.5	2.18	2.53	−0.7	5.62	na
Luxembourg	−6.5 Apr	+4.9 Q1	na	0.63	0.73	0.6	4.96	na
New Zealand	−3.6 May	−10.4 Q1	−7.0	1.31	1.28	1.9	7.90	6.34
Peru	+8.0 Apr	+0.8 Q1	−0.2	2.95	3.17	1.7	5.75	na
Philippines	−7.6 Apr	+5.6 Mar	+4.1	45.2	46.1	−0.5	5.94	na
Portugal	−29.3 Mar	−26.0 Apr	−8.5	0.63	0.73	−2.4	4.96	5.08
Slovakia	−1.1 Apr	−4.3 Mar	−3.2	19.1	24.6	−2.1	4.02	5.20
Slovenia	−3.4 Apr	−2.8 Apr	−4.0	0.63	0.73	−0.2	na	na

*Merchandise trade only. †*The Economist* poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.

Markets

Jul 3rd 2008
From The Economist print edition

Markets

	Index	% change on		
			Dec 31st 2007	
	Index Jul 2nd	one week	in local currency	in $ terms
United States (DJIA)	11,215.5	-5.0	-15.4	-15.4
United States (S&P 500)	1,261.5	-4.6	-14.1	-14.1
United States (NAScomp)	2,251.5	-6.2	-15.1	-15.1
Japan (Nikkei 225)	13,286.4	-3.9	-13.2	-8.6
Japan (Topix)	1,301.2	-3.3	-11.8	-7.2
China (SSEA)	2,781.1	-8.7	-49.6	-46.3
China (SSEB, $ terms)	207.7	-3.9	-46.7	-43.2
Britain (FTSE 100)	5,426.3	-4.2	-16.0	-15.9
Canada (S&P TSX)	14,034.1	-2.8	+1.5	-1.4
Euro area (FTSE Euro 100)	1,031.0	-5.2	-25.0	-18.6
Euro area (DJ STOXX 50)	3,288.5	-5.0	-25.3	-18.9
Austria (ATX)	3,800.7	-6.1	-15.8	-8.6
Belgium (Bel 20)	3,081.8	-8.3	-25.3	-19.0
France (CAC 40)	4,296.5	-5.3	-23.5	-17.0
Germany (DAX)*	6,305.4	-4.7	-21.8	-15.2
Greece (Athex Comp)	3,190.4	-11.0	-38.4	-33.1
Italy (S&P/MIB)	28,974.0	-3.4	-24.8	-18.4
Netherlands (AEX)	408.4	-7.1	-20.8	-14.1
Spain (Madrid SE)	1,279.0	-4.5	-22.1	-15.5
Czech Republic (PX)	1,471.4	-2.6	-18.9	-1.9
Denmark (OMXCB)	388.1	-4.7	-13.5	-6.2
Hungary (BUX)	20,216.7	-1.6	-22.9	-10.5
Norway (OSEAX)	531.4	-2.2	-6.8	-0.1
Poland (WIG)	40,420.0	-3.9	-27.4	-15.5
Russia (RTS, $ terms)	2,255.5	-2.4	-6.2	-1.5
Sweden (Aff.Gen)	265.7	-6.5	-22.0	-15.5
Switzerland (SMI)	6,843.8	-3.4	-19.3	-10.2
Turkey (ISE)	33,566.4	-10.7	-39.6	-42.8
Australia (All Ord.)	5,211.6	-2.8	-18.8	-10.8
Hong Kong (Hang Seng)	21,704.5	-4.1	-22.0	-22.0
India (BSE)	13,664.6	-3.9	-32.6	-38.5
Indonesia (JSX)	2,378.5	+1.6	-13.4	-11.7
Malaysia (KLSE)	1,153.7	-4.6	-20.2	-19.4
Pakistan (KSE)	12,126.1	-2.4	-13.9	-23.3
Singapore (STI)	2,906.2	-2.7	-16.1	-11.2
South Korea (KOSPI)	1,623.6	-5.5	-14.4	-22.7
Taiwan (TWI)	7,353.9	-6.4	-13.5	-7.7
Thailand (SET)	760.0	-2.4	-11.4	-10.7
Argentina (MERV)	2,033.0	-2.8	-5.5	-1.4
Brazil (BVSP)	61,106.0	-7.2	-4.4	+6.6
Chile (IGPA)	13,847.6	-7.3	-1.6	-5.1
Colombia (IGBC)	9,001.2	-3.1	-15.8	-7.3
Mexico (IPC)	28,680.8	-3.0	-2.9	+2.2
Venezuela (IBC)	37,506.5	+1.7	-1.0	-37.9
Egypt (Case 30)	10,041.9	-1.0	-4.1	-0.8
Israel (TA-100)	966.7	-5.5	-16.3	-1.5
Saudi Arabia (Tadawul)	9,467.7	-1.2	+19.3	+19.4
South Africa (JSE AS)	29,303.7	-2.2	+1.2	-11.5
Europe (FTSEurofirst 300)	1,167.9	-4.9	-22.5	-15.9
World, dev'd (MSCI)	1,375.4	-3.7	-13.4	-13.4
Emerging markets (MSCI)	1,057.2	-4.4	-15.1	-15.1
World, all (MSCI)	348.3	-3.8	-13.6	-13.6
World bonds (Citigroup)	768.2	+1.5	+5.2	+5.2
EMBI+ (JPMorgan)	429.9	-0.8	-0.9	-0.9
Hedge funds (HFRX)	1,302.0	-1.4	-2.1	-2.1
Volatility, US (VIX)	27.3	21.1	22.5	(levels)
CDSs, Eur (iTRAXX)†	105.2	+11.2	+108.1	+125.8

Foreign direct investment

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The 30 members of the mostly rich OECD made foreign direct investments (FDI) worth $1.82 trillion last year, well above the record set in 2000 (when a dollar was worth rather more). Direct investment flows into OECD countries also set a new record, rising by 31%, to $1.37 trillion. America remained both the biggest financier and the biggest recipient of direct investments, though its inflows fell from 2006. In smaller countries FDI figures are often swollen by one big merger. The sale of ABN AMRO to a group of foreign banks boosted the Netherlands' inward FDI to a record $99 billion. The appetite for international mergers has cooled somewhat since that deal. As a result, FDI flows are set to fall this year.